united states department of justice

REPORT

on the robinson-patman act

DEPARTMENT OF JUSTICE

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ROBINSON-PATMAN ACT

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PREFACE

Over the past months, the Administration has been engaged in a comprehensive review of the many statutes which regulate the nation's economic activity. As part of this effort, the Antitrust Division of the Department of Justice undertook the task of evaluating the effects of the Robinson-Patman Act, a 1936 amendment to the Clayton Act dealing with price discrimination in the sale of commodities in interstate commerce. The initial product of the Division's effort was the release, in the summer of 1975, of a White Paper and two draft statutes which discussed the repeal or reform of Robinson-Patman.

In response to the ensuing debate, the Department commenced an in-depth analysis of Robinson-Patman. At the same time the Domestic Council Review Group on Regulatory Reform decided to hold hearings on the operation of Robinson-Patman for the purpose of learning whether the Act should be retained, modified, or repealed. Over 20 persons testified at these hearings which took place on December 8, 9, and 10, 1975. Witnesses included members of the academic community, practicing attorneys, representatives of small business groups, businessmen, and present and former government officials.

Upon the conclusion of these hearings, Antitrust Division staff members began the preparation of this Report.

The ultimate views contained in this Report draw on those hearings, as well as hearings held in late 1975 and early 1976 by the Ad Hoc Subcommittee on the Antitrust Laws, the Robinson-Patman Act, and Related Matters of the U.S. House of Representatives Small Business Committee, and further research by the Antitrust Division. The Report is intended to provide officials of the Executive Branch, Members of Congress, and the public with a clearer understanding of the costs and benefits of a price discrimination statute to our complex economy and of the various possibilities for legislative action.

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Chapter I. INTRODUCTION

On June 19, 1936, the Robinson-Patman Act became law as an amendment to the antitrust laws. 1/ This Act was intended to prevent monopolization of the distributive process by halting price discrimination which might lead to the disappearance of the independent retailer and wholesaler. Price discrimination was seen not as a normal function of free market forces but as a tool of predatory sellers and buyers seeking to acquire, maintain and exercise monopoly power. The victims of price discrimination were thought to be the small independent retailers; the beneficiaries were thought to be the corporate chains. The basic solution which emerged from the legislative process was a statutory ban on all price discrimination injurious to competition except that justified by costs or the need to meet a competitive price.

A. The Statute Generally Described

The Robinson-Patman Act has two prohibitory sections, sections 1 and 3. Section 1 amends Section 2 of the Clayton Act and is usually referred to as Section 2 of Robinson-Patman. It is the most often enforced and can serve as the basis for a civil action by the FTC,

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1/ Act of June 19, 1936, c.592, 49 Stat. 1526. See text at Appendix B.

the Department of Justice or a private plaintiff. Section 3 is a criminal statute which can be enforced only by the Department of Justice; it repeats some of the prohibitions of Section 2 but also outlaws the sale of goods "at unreasonably low prices for the purpose of destroying competition or eliminating a competitor."

Section 2(a) prohibits discrimination in price by a seller where a sale of commodities of like grade and quality is made in interstate commerce. The prohibition applies only to those price discriminations whose effect "may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them."

Section 2(a) provides several defenses to the general prohibition. For example, a discrimination may be defended on the ground that the differential in price makes "only due allowance for differences in the cost of manufacture, sale, or delivery" resulting from differing quantities or methods in sale or delivery. This is commonly referred to as the "cost justification defense." The section also permits discriminations resulting from a changing condition affecting the market for the goods or their marketability. This allows the seller to cut prices on obsolete or deteriorating goods.

Section 2(b) provides that after a plaintiff makes out a prima facie case that the discrimination is unlawful, the defendant must then rebut the presumption of illegality. A proviso to Section 2(b) creates a "meeting competition" defense, which permits a seller to rebut the prima facie case by showing that his price reduction was intended to meet a competitor's lower price.

Section 2(c) outlaws certain payments made in lieu of brokerage, and Sections 2(d) and 2(e) prohibit, respectively, the granting of allowances for services or facilities provided by the purchaser, or the furnishing of any services or facilities involved in the processing or handling of the commodity in question, unless such concessions have been accorded "to all purchasers on proportionally equal terms." Unlike Section 2(a), these sections require no showing of injury to competition. Moreover, defenses to a violation of these sections are limited.

Section 2(f) makes it unlawful for a buyer engaged in interstate commerce, in the course of such commerce, knowingly to induce or receive a price discrimination which would be unlawful for a seller to grant.

Under existing liaison agreements between the Department of Justice and the Federal Trade Commission, the FTC has taken primary responsibility for civil enforcement of the Robinson-Patman Act, leaving the Department of Justice with responsibility for criminal prosecutions under Section 3. That section, never intended as a substantive addition to the Act, has rarely been invoked.

The number of FTC civil actions under Section 2 has declined in recent years. The FTC is presently considering whether to increase its Robinson-Patman enforcement. On the other hand, private suits under Robinson-Patman appear to have increased. 2/ One Review Group witness predicted 3/ that private enforcement of the Act will have the greatest impact upon the economy.

B. The Types of Price Discrimination to which the Robinson-Patman Act Applies.

Price discrimination, 4/ the basic concern of the Robinson-Patman Act, means in economic terms the sale of different units of a good or service at prices which differ by more than the cost of supplying those different units. Thus, selling units of equal cost at different prices is price discrimination, as is the sale of units of differing costs at the same price.

The Robinson-Patman Act does not regulate all types of price discrimination. For example, the Robinson-Patman Act applies only to the sale of goods in interstate commerce, and not to transactions involving

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2/ Testimony of Owen M. Johnson, Hearings before the Ad Hoc Subcommittee on Antitrust, the Robinson-Patman Act and Related Matters of the House Committee on Small Business, 94th Cong., 2nd Sess., pt. 2 at 204 (1976) (hereinafter cited as Subcommittee Hearings. The conclusions of the Ad Hoc Subcommittee are set forth in H.R. Rep. No. 94-1738, 94th Cong., 2nd Sess. (1976).

3/ Testimony of Donald A. Frederick, Hearings on the Robinson-Patman Act before the Domestic Council Review Group on Regulatory Reform, Tr. 380 (1975) (hereinafter cited as DCRG Hearings).

4/ The word "discrimination" has a pejorative connotation derived from its use in other contexts, e.g., racial or religious discrimination. A proper understanding of its use in economic terms requires a conscious effort to disassociate the word's social meanings.

services. Furthermore, the Act applies only to discrimination in which there is a price differential charged, and not to a transaction involving units of differing costs sold at the same price.

The statute prohibits only those price discriminations which have the required adverse effect upon competition. Where the price discrimination allegedly injures the competitors of the seller granting it, there is said to be "primary line injury." Where the effect of the price discrimination is alleged to injure the competitors of the buyer receiving the preferential discriminatory price, there is said to be "secondary line injury."

Primary line cases under Robinson-Patman occur where a multi-market seller lowers his price in a market with the effect of economic injury to his local competitors. Such conduct was widely believed to have furthered the Standard Oil and American Tobacco trusts. 5/

The chief objective of the Robinson-Patman Act, however, was not to prohibit primary line injury; that situation was already covered by the Clayton and Sherman Acts. Rather, the Act's main purpose was to prohibit price differentials which affected competition at the secondary line. The Act forbids sellers from charging discriminatory prices which are injurious to competition unless the differential is cost-justified or is a response to competition. In addition, discriminations disguised as brokerage or promotional allowances are absolutely prohibited. To complete the scheme, buyers are prohibited from knowingly inducing or receiving an unlawfully favorable price. This prohibited conduct was perceived as the tool by which the emerging chain stores, principally the Great Atlantic & Pacific Tea Company, were driving small retailers out of business.

5/ F. ROWE, PRICE DISCRIMINATION UNDER THE ROBINSON-PATMAN ACT 6 (1962).

C. The Question Presented

The Robinson-Patman Act is a piece of depression-era legislation, reflecting the social and economic concerns of that period. The 1930's saw rapidly falling prices and an increase in the mortality of businesses of all types and sizes. During this time much of the enacted legislation reflected a deep-seated belief that free competition was hopelessly inadequate to the task of regulating the market place. It was this period, for example, which spawned the National Recovery Administration, whose provisions combined the efforts of government and industry to raise prices and protect established relationships in distribution for the purpose of returning the country to full employment.

Congresses convened during this period were particularly sensitive to the argument that small retailers and their immediate suppliers were in danger of being eliminated by the development of mass merchandising techniques, and that, as a result, the public interest was threatened by a long run reduction in consumer choice and tendency toward monopoly.

The controversy surrounding the Robinson-Patman Act in the 1930's was intense; the debate pitted those who stressed the consumers' interests in low prices and efficiency in distribution against those who claimed that Robinson-Patman-type legislation was the last hope for the survival of the small businessman and a free market system. Debate of this sort has recurred throughout the history of the Robinson-Patman Act from the 1930's to the present. At one extreme supporters of the Act have viewed it as the "Magna Carta" of small business; at the other, opponents have regarded it as "thoroughly discredited." 6/ In recent years the debate

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6/ Elias, Robinson-Patman: Time For Rechiseling, 26 MERCER L. REV. 689, 689 (1975).

has assumed a new and important dimension which focuses the issue in more fundmental terms: does the Robinson-Patman Act have adverse effects on competition and consumers and, if so, does the Act, in fact, offer any concrete countervailing benefit to small businessmen which cannot be achieved by less harmful alternatives?

This Report will offer an answer to this question. The Report begins with an analysis of the social costs of Robinson-Patman: its effects upon pricing and efficiency in distribution and thus upon the consumer. Next, the Report describes the Act's genesis, its causal relation to social and economic conditions at the time of enactment and its legislative history. The Report then analyzes the Act's economic assumptions and current justifications to determine whether they are supportable in theory and in fact, and to determine further whether they establish goals capable of being achieved by Robinson-Patman. The Report concludes with a recommendation.

Chapter II. ANALYSIS OF THE EFFECT OF ROBINSON-PATMAN UPON COMPETITION, PRICES, EFFICIENCY AND THE CONSUMER

Fundamental to an understanding of Robinson-Patman is the fact that the Act places a complex series of legal restrictions on the central process of a market economy--the setting of prices between buyer and seller. Consequently, if Robinson-Patman does have an effect on business behavior--and if it had absolutely no effect there could be no justification for it--that effect is to distort prices from those that would otherwise prevail in the marketplace.

As recent experiences with wage and price controls have demonstrated, governmental tampering with the market can lead to unforeseen results which have an adverse effect on workers, businesses, and the consuming public. It should not be surprising, therefore, that Robinson-Patman can be shown to have many adverse effects on the economy. To be sure, there are some who do not recognize these effects or who argue that they are outweighed by benefits to specific sectors of the economy, notably small business; to competition by preventing increased concentration in a line of commerce; and to public values in general by establishing as a legal norm the concept of "fair dealing" in pricing. But any discussion of the benefits of Robinson-Patman can be made only with a clear understanding of the burdens that the statute places on American economic activity. This section of the Report makes such an analysis, starting first with a discussion of the Act's legal impact upon businessmen, then proceeding to a description of the actual effects of the statute on the economy.

A. <u>The Legal Requirements and Risks Under Robinson-Patman</u>

The effect of Robinson-Patman upon pricing in the economy can best be gauged by examining the decision-making process which a reasonable businessman contemplating an adjustment in prices might follow when faced with legal advice concerning Robinson-Patman liability. To the extent that that businessman sees extensive exposure to liability under the statute as a result of his pricing strategy, it is reasonable to conclude that his inclination to adjust prices downward on a selective basis will be reduced.

What such a reasonable businessman will discover is that Robinson-Patman weighs heavily in favor of those who would attack a competitor's non-uniform price change and against a firm which dares to lower its prices to less than all customers. A complaining party may easily make out a prima facie case; if that party can show any differential in price, the law creates a virtual presumption of illegality. Once a prima facie case has been made out, a seller accused of unlawful price discrimination must show that he meets one of the statutory defenses. But the defenses are exceedingly difficult to prove. Moreover, to some charges under the Act, no defense whatsoever is allowed. Finally, the reasonable businessman will learn that, if found in violation of the Act, serious sanctions can be imposed without regard to actual damages incurred by competitors, actual harm to competition, or benefit to the discriminating firm received through the violation. Under such circumstances, to refrain from the price reduction is a reasonable choice.

1. The Complaining Party Can Easily Establish a Prima Facie Case Against the Selective Price Reductions of Sellers

On its face, the statute requires a plaintiff, in order to make out his case, to prove a discrimination in price and an adverse effect upon competition. Under the Act as interpreted, however, a complaining party need not prove much more than the fact of a difference in price.

The term "price discrimination" has been interpreted to mean a price differential of any amount. In FTC v. Anheuser-Busch, Inc. 7 / the Supreme Court held that price discrimination was synonymous with difference in price. 8 /

> We are convinced that, whatever may be said with respect to the rest of §§2(a) and 2(b) -- and we say nothing here -- there are no overtones of business buccaneering in the §2(a) phrase "discriminate in price." Rather, a price discrimination within the meaning of that provision is merely a price difference.

Thus, the complaining party's task is made simpler by the lack of any need to prove that the amount of the price discrimination is economically significant.

The relative ease with which plaintiff can prove the second element in his case -- adverse effect upon competition -- depends upon whether primary or secondary line injury is alleged. In secondary line cases, the Robinson-Patman Act proscribes price differentials which "injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them." Secondary line cases under the Act permit the requisite injury to be proved by easily drawn inferences.

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7 / 363 U.S. 536 (1960).

8 / Id. at 549.

The leading case, FTC v. Morton Salt Co., 9/ permits inference of competitive injury to be drawn from the existence of a price differential sufficiently large to affect resale price levels. The respondent in that case, a manufacturer of table salt, sold its product on a standard quantity discount system available to all customers; the purchase price depended solely upon the quantity bought. 10/ The Court held that the statute's requirement of injury to competition was satisfied by the FTC's finding that the price differential was "sufficient in amount to influence . . . resale prices." 11/ The result, the Court noted, was compelled by Congress' use of the incipiency standard; a complaining party need not show actual harm to competition from the discrimination but merely "a reasonable possibility that [it] 'may' have such an effect." 12/ It then follows that prices sufficiently disparate to be reflected in resale prices will be found to have an

9/ 334 U.S. 37 (1948).

10/ Id. at 41.

11/ Id. at 47.

12/ Id. at 46, quoting Corn Products Refining Co. v. FTC, 324 U.S. 726, 742 (1945).

adverse effect upon competition. 13/

Once an inference of secondary line competitive injury is established under the Morton Salt doctrine, direct evidence to the contrary may not overcome the Morton Salt inference. For example, the direct admission of the disfavored customer that he was in no way injured by the alleged price discrimination has been held insufficient to negate the inference of competitive injury which arises out of the mere fact of the discrimination itself. In United Biscuit Co. of America v. FTC, 14/ an FTC proceeding against a manufacturer of cookies and crackers who sold to

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13/ The Morton Salt doctrine has been followed in a long line of opinions which infer adverse effect upon competition from price differentials affecting resale price. E.g., Beatrice Food Co., 76 F.T.C. 719 (1969), aff'd sub. nom. Kroger Co. v. FTC, 438 F.2d 1372 (6th Cir.) cert. denied 404 U.S. 871 (1971); Standard Motor Products, Inc. v. FTC, 265 F.2d 674 (2nd Cir.), cert. denied 361 U.S. 826 (1959); C.E. Niehoff & Co. v. FTC, 241 F.2d 37 (7th Cir. 1957); Moog Industries, Inc. v. FTC, 238 F.2d 43 (8th Cir. 1956), aff'd per curiam 355 U.S. 411 (1958).

There are some lower court and FTC cases, however, which inquire beyond the Morton Salt inference to consider whether actual injury to competition is reasonably evidenced. For example, in Fred Bronner Corp., 57 F.T.C. 771 (1960), the Commission found that a 3% price differential had no adverse effect on competition, even though profits in the industry were small, between 2% and 5%. Furthermore, at least one appellate court has suggested that no injury to competition occurs where the lower price is available to the disfavored customer from another supplier. Tri-Valley Packing Ass'n v. FTC, 329 F.2d 694 (9th Cir. 1964), on remand, 70 F.T.C. 223 (1966), mod. and aff'd sub nom. Tri Valley Growers v. FTC, 411 F.2d 985 (9th Cir.) cert. denied, 396 U.S. 929 (1969).

14/ 350 F.2d 615 (7th Cir. 1965), aff'g 60 F.T.C. 1893 (1962), cert. denied 383 U.S. 926 (1966).

various retail grocery store customers, the complaint charged that the respondent discriminated in favor of its chain store customers to the detriment of its independent retail customers, thereby injuring competition. At the proceeding, however, the majority of independent retail customers admitted that any actual injury to their business was highly unlikely. On appeal from the resulting cease and desist order, the Seventh Circuit held that the incipiency standard of the Robinson-Patman Act allowed the FTC to infer injury to competition even in the face of direct evidence to the contrary. 15 /

If the product to which the price discrimination applies constitutes but a small portion of the disfavored customer's business, the possibility of any adverse effect upon a competitor or upon competition is slight. Nevertheless, the FTC has held that relative unimportance of the product to the disfavored customer's business will not rebut the Morton Salt inference. In Moog Industries, Inc. v. FTC, 16/ the court held that the FTC was entitled to infer injury to competition notwithstanding testimony by disfavored customers that the discriminating seller's product accounted for a small portion of their business and that, therefore, those customers did not feel that they had been competitively injured.

Finally, evidence that additional distributive functions performed by favored customers account for the difference in prices will not dispel

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15/ See also Moog Industries, Inc. v. FTC, 238 F.2d 43 (8th Cir. 1956), aff'd per curiam 355 U.S. 411 (1958); Standard Motor Products, Inc. v. FTC, 266 F.2d 674 (2d Cir.), cert. denied 361 U.S. 826 (1959).

16/ 238 F.2d 43 (8th Cir. 1956), aff'd per curiam 355 U.S. 411 (1958).

the inference of competitive injury. In an automotive parts case, 17/ the respondent-manufacturer offered evidence to prove that its different prices to different warehouse distributors depended upon the nature and extent of distribution functions performed by those customers. For example, respondent offered evidence to prove that a purchasing warehouse dealer who resold the product directly to automotive dealers incurred 4% greater expense than those warehouse dealers who resold to jobbers who in turn resold to automotive dealers. This increased cost of redistribution, it was argued, in all cases equalled or exceeded the discount actually given to the warehouse distributor, and that the favored distributor therefore gained no competitive advantage. The Commission, whose ruling was sustained by the Seventh Circuit, refused to consider such evidence on the question of competitive injury. It was held that to allow such evidence to disprove injury to competition would be to allow a manufacturer-seller to subsidize some of its customers' greater cost of doing business. 18/

The total effect of the majority of the secondary line cases is to create a virtually irrebutable presumption that any price discrimination is injurious to competition. Thus, the legal advice to a businessman contemplating a price cut to less than all customers will likely persuade the client that if he proceeds, it is at his considerable peril. As was pointed out by an antitrust lawyer testifying before the Review Group,

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17/ Purolator Products, Inc. v. FTC, 352 F.2d 874 (7th Cir. 1965), cert. denied, 389 U.S. 1047 (1968).

18/ Id. at 882.

a responsible attorney considering changes in his client's pricing strategy can only 19/

> advise [his] client that if he does price discriminate within a given market, it is quite likely that the court will find this discrimination injurious to competition and that he will have to either rely on one of the defenses or suffer the consequences of treble damage liability.

In the primary line situation, where the complaining party alleges injury to competition at the level of the firm granting the discriminatory price, i.e., at the seller's level, injurious effect may not be inferred as easily as in secondary line cases, but the requirement of adverse effect upon competition is still easily satisfied. In Utah Pie Co. v. Continental Baking Co., 20/ the plaintiff was a local firm which had for 30 years baked and distributed its pies in Utah and surrounding states. Three national firms sought to enter the local market with frozen dessert pies, but the plaintiff, due to the location of its plant in Salt Lake City, was able quickly to add frozen pies to its product line and market them at prices below those of the national firms. Plaintiff soon became the dominant firm, with 66.5% of the market. The national firms, who challenged the plaintiff's position by reducing prices to local retail outlets, were found to have injured competition by causing a "deteriorating price structure." 21/ Yet an objective view of the facts suggests

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19/ Testimony of Christian L. Campbell, DCRG Hearings, Tr. 128.

20/ 386 U.S. 685 (1967).

21/ Id. at 690.

neither serious injury to Utah Pie nor to competition resulting from the discrimination. Prior to market penetration by the defendants, Utah Pie had a 66.5% market share; thereafter, its market share remained a dominant 45%. Utah Pie's sales volume increased over the period of price discrimination. Price competition from the defendants forced plaintiff to lower its prices over a three year period from $4.14 to $2.75 per dozen, reducing plaintiff's profits but still returning Utah Pie a net profit of 15% on sales of $589,000. In short, the plaintiff lost a measure of market dominance and reduced its profits, but, far from being eliminated, remained a profitable firm with by far the largest share of the local market. 22/

Again, the great likelihood is that a businessman considering geographic price discrimination to enter new markets will be given legal advice which has the necessary effect of instilling caution in pricing. 23/

> The result of Utah Pie is that when you have a client who is considering coming into a local market you have to advise him that, under the Act, it is basically an all or nothing calculus.
>
> If he comes into a local market and prices at a lower rate than he is pricing elsewhere, he is not going very likely to be found not liable under the no injury to competition standard; under Utah Pie, he is very susceptible to antitrust challenge.
>
> And he can almost expect that such challenge will be made. This has got to preserve anticompetitive situations in local markets, because most sellers are not willing to make across-the-board price reductions just to enter a single market.

22/ It has been argued that the statute, properly interpreted, does allow price reductions in a selected geographic area in order to gain entry into the market. Prepared statement of Earl W. Kinter at 6, DCRG Hearings, citing FTC v. Sun Oil Co., 371 U.S. 505 (1963), a secondary line case, and Hruby Distributing Co., 61 F.T.C. 1437 (1962), a § 2(c) brokerage case, in support of this proposition.

23/ Testimony of Christian L. Campbell, DCRG Hearings, Tr. 126.

> So, in essence, in this primary line case situation, you have legal advice coming down, possibly saying there is a chance that a court may find his conduct not injurious to competition, but the safest path always is to maintain prices at a uniform level.

This uncertainty facing a businessman contemplating entry into new markets through geographic price reduction was echoed by a Commissioner, who admitted that: 24/

> I am still not even certain, for example, whether a new entrant in a market can, for a while, price lower there than elsewhere.

In both primary and secondary line cases, the issue of injury to competition has been resolved by focusing on damage, and not necessarily fatal damage, to a specific firm or firms, and not on the effects upon the process of competition. Businessmen realize that if it can be shown that any firm, as a result of the price differential in question, will suffer loss of profits or market share, the likelihood of liability is extremely high. Under the Act as presently interpreted, the complaining party: 25/

> can establish injury to competition merely by showing that injury to a single competitor has occurred.
>
> And it is almost impossible in a practical situation to have a case where injury to a single competitor has not occurred.

24/ Statement of Stephen Nye, Subcommittee Hearings, pt. 3 at 101.

25/ Testimony of Christian L. Campbell, DCRG Hearings, Tr. 120-21.

2. Defenses to a Charge of Price Discrimination Are Difficult to Prove.

Having created a virtual presumption of illegality for price discrimination, Congress could have permitted defenses which could realistically be met by firms facing liability for their pricing activities. This did not happen. As interpreted, Robinson-Patman defenses are difficult to prove because their requirements are not consonant with business realities.

The first defense, cost justification, arises out of the proviso to Section 2(a) of the Clayton Act which provides "[t]hat nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered." 26/ Even accepting the questionable assumption that the price of the commodity depends solely upon its cost, 27/ the cost defense is as difficult to prove as the prima facie case is easy to establish. The history of the cost justification defense before the FTC and the courts shows hostility to its use; the Commission for many years insisted upon meticulously exact cost data in order to sustain the defense. In an attempt to facilitate compliance with its standards, the Commission established an advisory committee on cost justification in order to provide businessmen with cost

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26/ 15 U.S.C. § 13(a).

27/ Economists point out that the cost of a commodity is but one determinant of its final price, and that attempting to link all price differentials with cost changes distorts legitimate pricing practices. See Chapter IV(A). *infra* p. 159 .

accounting standards by which the cost justification defense was to be measured, but the committee's final report and recommendation were never acted upon by the FTC. 28/ While the report was never endorsed by the Commission, one of its suggested approaches to cost justification, the approval of broad customer groupings for cost data accumulation, has been accepted by the Supreme Court. In United States v. Borden Co. 29/, the Court recognized that it would be impossible for a seller to prepare cost data showing its justification for each price granted to every individual purchaser. The Court held that purchasers having similar characteristics with respect to the cost of delivering goods to them might be grouped together for purposes of cost justification.

Ironically, neither respondent involved in the Borden case was able to take advantage of the supposedly liberalized requirements, since each was found to have made faulty customer groupings. Borden, for example, grouped together all independents for purposes of comparing cost differences between sales to them and sales to chains. The Court held that, since some independents had sales volumes higher than some of the individual chain outlets, such grouping was fatally defective. The result in Borden exemplifies one difficulty with the cost justification defense; a seller may, in good faith, prepare an elaborate cost justification defense only to find that, by the erroneous inclusion of one or more purchasers in the same class, he has unwittingly violated the Act.

A second deficiency with the cost justification defense is that no seller can be sure exactly what costs will be deemed material to the

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28/ ADVISORY COMMITTEE TO THE FEDERAL TRADE COMMISSION, REPORT ON COST JUSTIFICATION (1956).

29/ 370 U.S. 460 (1962).

granting of a discount to a particular purchaser. It has been held, for example, that the cost savings associated with billing large sales to mass purchasers may not be significant enough to justify a reduced price to any such purchaser. 30/

Similarly, the desire of a seller to grant a large purchaser a discount representing advertising expense assumed by the large purchaser is often thwarted by the difficulty of proving such a cost justification defense. As with the Borden-type problem of customer grouping, the seller may find that he has made incorrect groupings for purposes of allocating the advertising expense savings. Furthermore, he may find that the savings involved are not significant enough, in the Commission's view, to justify the discount granted. 31/

Finally, the Federal Trade Commission has determined that return on capital facilities dedicated to selling to one class of customers but not to another may not be taken into account in justifying a price cut to a purchaser in the latter class. In Thompson Products, Inc., 32/ the manufacturer sold auto parts both to wholesalers in the replacement parts industry and directly to the major auto manufacturers for use as original equipment. The respondent maintained a separate facility for storage and

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30/ Alhambra Motor Parts, 68 F.T.C. 1039, 1080 (1965); National Parts Warehouse, 63 F.T.C. 1692 (1963), aff'd sub nom. General Auto Supplies, Inc. v. FTC, 346 F.2d 311 (7th Cir.), cert. denied, 382 U.S. 923 (1965).

31/ C. E. Niehoff & Co., 51 F.T.C. 1114 (1955), aff'd, 241 F.2d 37 (7th Cir. 1957), vacated and remanded per curiam, 355 U.S. 411 (1958).

32/ 55 F.T.C. 1252 (1959).

distribution of those parts which were sold to the after market industry; no such facilities were needed with respect to sales to the original equipment market. The Commission held that a reasonable rate of return on those capital facilities could not be taken into account to justify a discount on sales in the original equipment markets, noting that some of the parts sold in both lines of business were the same, even though they passed through different channels of distribution.

Even if the seller has cost savings cognizable under the Act, he must compute them with unrealistic accuracy. While the standards applied to accounting studies for the purpose of cost justification have become somewhat more reasonable, the Commission still insists upon studies based upon actual, historical cost rather than estimated future cost, and will allow but a small margin of error in the computations. In Beatrice Foods Co., 33/, the seller of dairy products performed an elaborate study to justify price cuts given to a large purchaser, the Kroger Company. A key part of the study involved computation of time savings involved in delivering large orders to large purchasers. The study was rejected, however, on the grounds that the estimates of time involved in selling were made too long after the actual period of discrimination, that employees reporting stop times were likely to exaggerate to their employer the amount of time spent on each call, and that conditions had changed substantially over the routes to which the time study applied.

Not only must a cost justification defense meet the high standards of methodology imposed by the FTC, but the result of such study must prove

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33/ 76 F.T.C. 719 (1969), aff'd sub nom. Kroger Co. v. FTC, 438 F.2d 1372 (6th Cir.) cert. denied 404 U.S. 871 (1971).

that the cost savings associated with dealing with a particular customer account for nearly all of the discount granted the customer. The FTC purports to apply a de minimis rule, which holds that if the cost justified differential and the actual differential contested are so close that the difference is insignificant, the cost justification defense will have been established. The precise limits of the rule have not been established, but it appears that if even a small portion of the actual price differential is non-cost-justified, the entire defense may fail. In American Metal Products Co. 34/ it was held that where a seller makes a bona-fide effort to demonstrate the cost justification for a price differential, the fact that less than one percent of the total price cut is not cost justified does not operate to deny the defense to the seller. But in Thompson Products, Inc. 35/ the Commission held that where the seller's discounts to large auto manufacturers were between three and seven percent greater than what a perfect cost justification study would show, the cost justification defense was inapplicable.

The difficulty of complying with the FTC's rigid cost justification requirements, plus the expense of collecting data through methods foreign to most accountants and businessmen, 36/ make the barriers to practical utilization of the defense almost insurmountable.

34/ 60 F.T.C. 1667 (1962) (initial decision).

35/ 55 F.T.C. 1252 (1959).

36/ See testimony of Paul H. La Rue, discussed in Section B. (1)(a), infra at page 42.

The other major defense to a charge of price discrimination, the meeting competition defense, arises out of the proviso to Section 2(b) of the Clayton Act which provides: 37/

> That nothing herein contained shall prevent a seller rebutting the prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor.

Not until 1963 did the FTC rule that a price cut was justified under Section 2(b). 38/ Thereafter, the Commission's interpretation of the defense has tended to restrict its application. Indeed, it took an appeal to the First Circuit, Forster Mfg. Co. v. FTC, 39/ to overturn the Commission's rule that a seller seeking to rely on the meeting competition defense must have "proof positive" of the exact competitor and price whose competition the respondent was seeking to meet. Even after the First Circuit's ruling in Forster Mfg. Co., the seller may not safely rely upon oral representations by purchasers that a competing seller is offering a lower price. The Act requires that a seller be a judge of his customer's credibility, and that the seller "investigate or verify" the lower offer which it is seeking to meet. 40/

To avail himself of the meeting competition defense, a seller must consider whether the price that he is seeking to meet is "lawful" or

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37/ 15 U.S.C. §13(b).

38/ SECTION OF ANTITRUST LAW AMERICAN BAR ASS'N., ANTITRUST LAW DEVELOPMENTS 144 (1975).

39/ 335 F.2d 47 (1st Cir. 1964), cert. denied, 380 U.S. 906 (1965).

40/ Viviano Macaroni Co. v. FTC, 411 F.2d 255 (3rd Cir. 1969).

"unlawful" under the Robinson-Patman Act. In Standard Oil Co. v. FTC, 41 / the Supreme Court's opinion referred to the defense as contemplating the meeting of a "lawful" price. For years the FTC required that the party seeking to invoke the defense prove that the price it was seeking to meet was, in fact, lawful. 42 / An appellate opinion, however, interpreted the Supreme Court's opinion as requiring merely that the seller be meeting a price which he did not know was unlawful. That opinion would seem to negate the FTC's interpretation that the burden of proof concerning legality of the price rests upon the seller. 43 / But if a seller knows or has reason to know a competing price is unlawful, the law requires the seller to engage in litigation rather than competition.

Risk also attends a seller's decision to meet competition by adopting an entire pricing system for that purpose rather than by specific competitive price cuts. The Commission asserts that a uniform change in the seller's total pricing system will not satisfy the meeting competition defense. 44 / There is a split authority among the various circuits. A Second Circuit

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41 / 340 U.S. 231 (1951).

42/ Tri-Valley Packing Ass'n., 60 F.T.C. 1134 (1962), rev'd on other grounds, 329 F.2d 694 (9th Cir. 1964).

43 / Standard Oil Co. v. Brown, 238 F.2d 54 (5th Cir. 1956).

44 / Knoll Int'l, Inc., [1970-1973 Transfer Binder] CCH TRADE REG. REP. ¶19,768 (FTC 1971).

opinion is in accord with the view expressed by the FTC. 45 / The Fifth Circuit, on the other hand, has held that, at least where a new competitor in the market seeks to establish a viable market share, the Act does not necessarily prohibit the use of pricing systems to meet competition. 46 / A subsequent Fifth Circuit opinion, however, casts doubt upon the ability of a seller to rely on the meeting competition defense when a pricing system is involved. In Surprise Brassiere Co. v. FTC, 47 / the court indicated that, where possible, a seller seeking to meet competition must limit his actions to the narrowest possible response.

Finally, under the Act as interpreted a seller may "meet but not beat" a competitor's price. For example, in National Dairy Products Corp., 48 / the FTC held that a seller of milk products had failed to establish a meeting competition defense when the record showed that the seller, in response to a competitor's price cuts, had undercut, rather than simply met, his competitor's price. 49 / The "meet but not beat" rule moderates potential price competition; the two competitors' prices, assuming compliance with the Act, will be identical. Of course, the requirement also exposes the seller to liability if he makes a mistake by

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45 / Standard Motor Prods., Inc. v. FTC, 265 F.2d 674 (2nd Cir.) cert. denied, 361 U.S. 826 (1959).

46 / Callaway Mills Co. v. FTC, 362 F.2d 435 (5th Cir. 1966).

47 / 406 F.2d 711 (5th Cir. 1969).

48 / 70 F.T.C. 79 (1966), aff'd, 395 F.2d 517 (7th Cir.), cert. denied, 393 U.S. 977 (1968).

49 / Id. at 198.

going "too low" in response to price competition. This risk may cause the seller either to withhold a response or to check with his competitor. Either course is undesirable; the latter would likely violate the Sherman Act.

The Commission is also of the view that the meeting competition defense is available only when a seller who cuts prices is attempting to retain present customers and not when he is seeking to acquire new customers. In Sunshine Biscuits, Inc., 50/ the meeting competition defense was held inapplicable to a seller seeking to acquire new wholesale customers by promotional pricing. While the Seventh Circuit rejected that interpretation, finding it "economically unsound" 51/, the Second Circuit has apparently accepted the Commission's interpretation of the defense. 52/ The FTC thereafter announced that it intended, in all cases, to limit the use of the meeting competition defense to defensive situations. 53/

Even the defensive use of the meeting of competition defense may expose a seller to liability where he cuts prices, not to meet his own competition but to help a customer meet his competition. In FTC v. Sun Oil Co., 54/ a gasoline refiner granted a reduction in price to one of

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50/ 59 F.T.C. 674 (1961), rev'd, 306 F.2d 48 (7th Cir. 1962).

51/ 306 F.2d at 52.

52/ Standard Motor Prods., Inc. v. FTC, 265 F.2d 674, 677 (2nd Cir.), cert. denied, 361 U.S. 826 (1959).

53/ FTC Press Release (Nov. 23, 1962, 1 CCH TRADE REG. REP ¶ 3345.52).

54/ 371 U.S. 505 (1963).

its independently owned service station customers, who was faced with price competition from a nearby service station selling a competitive brand of gasoline. The Supreme Court held that the meeting competition defense of Section 2(b) was not intended to cover the situation where a supplier gives a discount to help a customer meet competition.

The practical difficulty of establishing defenses to Robinson-Patman charges thus deters a rational businessman from engaging in selective price reductions. After a businessman has been told by legal counsel that the law favors any injured party wishing to attack his pricing policy, he must further be told that his defenses provide at best uncertain protection. As one eminent antitrust and Robinson-Patman Act practitioner testified, a seller can never be sure whether his cost justification study, no matter how diligently prepared, will satisfy the FTC. Furthermore, the execution of such a study involves methods foreign to accountants and businessmen, and requires extensive supervision by attorneys. 55/ Similarly, the difficulties facing a seller considering reliance on the meeting competition defense are enormous: ". . . a salesman is almost required to become a lawyer in order to know how he can meet competition and stay within the law." 56/ The average businessman may resolve doubts over the legality of price cutting by maintaining the higher price.

55/ Testimony of Paul H. La Rue, DCRG Hearings, Tr. 205-206.

56/ Id. at 207.

3. Certain Pricing Practices Are Per Se Illegal Without a Showing of Competitive Harm

While the statutory defenses to a charge of price discrimination are complex and unreliable, there are sections of the Robinson-Patman Act which prohibit pricing activity without regard to effect upon competition and which allow only limited or no defenses. Section 2(c) of the Act makes it unlawful for either party to a transaction to: 57 /

> pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other party to such transaction or to an agent, representative, or other intermediary therein where such intermediary is acting in fact for or in behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid.

Section 2(d) and (e) 58 / prohibit a seller from granting a customer advertising or promotional allowances or services unless such benefits are made available to all customers on a proportionally equal basis.

These sections were intended to prevent the circumvention of the Act's prohibition of discriminatory discounts through the devices of "dummy" brokerage payments or promotional allowances granted or received in lieu of direct discounts. Where violation of any of these sections is charged, however, the complaining party need not prove any adverse effect upon competition. 59 / Moreover, neither statutory defense is

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57 / 15 U.S.C. § 13(c).

58 / 15 U.S.C. § 13(d), (e).

59 / FTC v. Simplicity Pattern Co., 360 U.S. 55, 65 (1959).

available to a party charged under Section 2(c); only the meeting competition defense may be interposed in cases involving Section 2(d) or (e). 60/ Thus, while the brokerage and promotional allowance provisions of the Act prohibit activity which is economically indistinguishable from overt price reductions, a respondent charged under any of those sections may not argue the absence of injurious effect upon competition, nor may he avail himself of the full range of statutory defenses.

Sections 2(d) and (e) permit a seller to grant advertising or promotional allowances only if such benefits are made available to all customers on a proportionally equal basis. FTC and judicial attempts to implement the sections have created a complex scheme of regulation governing the promotional process.

The Supreme Court in Fred Meyer, Inc. v. FTC, 61/ held that all retailers in competition with one another, whether they purchase directly from the manufacturer or through an intermediary, must receive the benefit of proportional allowances, if a violation of Section 2(d) or (e) is to be avoided. In response to the Court's suggestion that guidelines would be helpful, the Commission in 1969 promulgated guides for advertising allowances and other merchandising payments and services. 62/ The

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60/ FTC v. Henry Broch & Co., 363 U.S. 166 (1960); FTC v. Simplicity Pattern, 360 U.S. 55 (1959).

61/ 390 U.S. 341 (1968).

62/ 16 C.F.R. § 240.1 et seq. (1975).

guidelines present a bewildering array of regulations with which the seller must comply. Among these regulations is the requirement that sellers police the conduct of intermediaries to insure that any promotional allowance is, in fact, passed through to the retailer since the definition of "customers," entitled under Sections 2(d) and (e) to receive equal allowances, includes any buyer of the seller's product who purchases "from or through a wholesaler or other intermediate reseller." 63/ Should the intermediary fail to pass the allowance on, it is the seller who may be held responsible.

Furthermore, under the FTC's regulations, a seller wishing to engage in promotion, through promotional allowances covered by Sections 2(d) and (e), must forebear implementation until all promotion can take place in accordance with a "plan." 64/ While the Commission does not require a formal written plan, it warns that a seller "would be well advised to put his plan in writing." 65/ A seller's plan must provide for affirmative action to inform <u>all</u> of his competing customers that such a plan exists, and must call for communication to such customers of the availability of the allowances. 66/

63/ 16 C.F.R. § 240.3(a) (1975).

64/ 16 C.F.R. § 240.6 (1975).

65/ <u>Id</u>.

66/ 16 C.F.R. § 240.6(b) (1975).

Even if the seller's promotional plan otherwise satisfies the requirements of the FTC's regulations, deficiencies in application of the plan may put the seller in violation of the Act. In House of Lords, Inc. 67/ a manufacturer of women's apparel offered to pay its customers approximately 50 percent of the cost of placing advertisements in newspapers and magazines. The Commission decided that the terms of the program were not available on a proportionally equal basis, and thus were violative of Section 2(d), since some of the customers were too small to afford any advertisement in newspapers or magazines, even if 50 percent of the cost were paid by the seller. 68/

67/ 69 F.T.C. 44 (1966).

68/ Id. at 79.

4. Buyers Are Exposed to Liability for Hard Bargaining Over Price

Under Section 2(f) of the Act, a buyer is liable for the knowing inducement or receipt of a price discrimination unlawful under Section 2(a). While scienter is usually a difficult matter to prove, the burden of proof with respect to knowledge was considerably lightened by the Supreme Court's opinion in Automatic Canteen Co. of America v. FTC, 69/ which allowed the Commission to rely on "trade experience" to show that the buyer should have recognized that a particular price received was unlawful. After Automatic Canteen, buyers have been found liable under Section 2(f) where the FTC showed, for example, that the buyer knew or should have known that the seller's discounts were not cost justified, 70/ that the buyer regularly used pressure to extract concessions, 71/ or that the seller protested that the requested discount would be discriminatory. 72/

As with Section 2(a), the plaintiff's burden under Section 2(f) is light. The buyer liability provision completes the Act's control of the distributive process by exposing both parties to a sales transaction to liability. The buyer liability provision, moreover, strikes at a process which is fundamental to a competitive market: the process by which each buyer negotiates for itself the best possible price. It

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69/ 346 U.S. 61 (1953).

70/ Kroger Co. v. FTC, 438 F.2d 1372 (6th Cir.), cert. denied, 404 U.S. 871 (1971).

71/ Fred Meyer, Inc. v. FTC, 359 F.2d 351, 363 (9th Cir. 1966), cert. denied, 386 U.S. 908 (1967).

72/ Giant Food v. FTC, 307 F.2d 184, 187 (D.C. Cir. 1962), cert. denied, 372 U.S. 910 (1963).

was, of course, the intent of the statute's drafters to discourage the use of coercive buyer pressure. Section 2(f), however, is not limited to such situations and operates without regard to the relative market power of the parties. The Section thus instills extreme caution in buyers negotiating for price breaks which, if obtained, might arguably subject them to liability under Section 2(f).

5. Pricing Practices of Sellers and Buyers Are Constrained by Overly Broad Injunctive Relief and Punitive Damages

Broad exposure to liability under the Robinson-Patman Act means that sellers and buyers are also exposed to that Act's costly sanctions. Under Robinson-Patman, there are two immediate consequences of violation of the Act: 73/ in an FTC proceeding a firm can be subjected to broad injunctive relief; in a private action a firm can in addition be made to pay treble damages to a complainant. As will be shown, either of these sanctions can impose serious costs on competitors found to violate the Act.

A respondent found to have violated the Robinson-Patman Act in an FTC proceeding frequently will be subjected to a cease and desist order much broader than the facts underlying the actual violation. In the most extensive analysis of FTC orders under the Robinson-Patman Act to date, 74/ one commentator found that virtually all cease and

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73/ Criminal violations of § 3 are punishable by imprisonment of up to one year and a fine of $5000. 15 U.S.C. § 13a. As previously stated, the Act's criminal provisions have rarely been used.

74/ Kauper, Cease and Desist: The History, Effect, and Scope of Clayton Act Orders of The Federal Trade Commission, 66 MICH. L. REV. 1095 (1968).

desist orders studied were of perpetual duration. Such orders would extend over the life of the firm regardless of changes in conditions or competitive environment. Similarly, many orders failed to limit their prohibitions of discriminatory pricing to the particular product which had been the subject of the FTC action. Finally, many orders failed to reflect the geographic limitations of the underlying action. Each violation of such orders may subject a firm to a fine of $10,000 with each day of violation constituting a separate violation. 75/

Upon advice of counsel, therefore, a businessman must consider the cost to his entire business of a pricing action perhaps limited to a single customer, a single market and a short period of time. The risk of a broad and unconditional order applying to his pricing practices in all markets, violation of which may be tremendously expensive, may well convince him to avoid selective price reductions.

In private litigation, the risk to sellers and buyers flows from the possible award of substantial money damages to the plaintiff. The award of damages in many jurisdictions does not require proof of actual injury. Damages, in these jurisdictions, are computed by multiplying the amount of the discrimination times the number of goods which the disfavored purchaser has acquired. The result, of course, is to place control of the size of the damage award in the hands of the prospective plantiff. 76/

75/ 15 U.S.C. § 45(1) (Supp. IV 1974).

76/ Fowler Mfg. Co. v. Gorlick, 415 F.2d 1248 (9th Cir. 1969); Elizabeth Arden Sales Corp. v. Gus Blass Co., 150 F.2d 988 (8th Cir. 1945).

Compounding the problem is the fact that, since Section 2 of the Robinson-Patman Act is designated as one of the antitrust laws, the award so computed is then tripled. 77/ The effect of this increased award is to magnify in a punitive manner the adverse effects of what may have been a good faith error in pricing. Moreover, the treble damage provision plus the possible award of attorney's fees makes potential awards large enough to encourage, under a contingency fee arrangement, litigation of questionable merit. Thus, a businessman must consider the fact that, if found to be in violation of the Act, the sanction imposed will have little relationship either to actual injury done to his competitors or to any benefit to him as a result of the price reduction. The mere threat of a treble damage complaint may intimidate a firm, causing it to withhold or withdraw price reductions.

6. The Overall Effect of Robinson-Patman Is To Instill Extreme Pricing Caution in Sellers and Buyers

The Robinson-Patman Act creates an overwhelming legal barrier for those firms contemplating price adjustment in response to specific competitive demands by less than all customers. The charging of prices sufficiently different in amount to affect resale prices creates a virtual presumption of illegality and rebuttal of that presumption is difficult if not impossible. The affirmative defenses are difficult to prove and require accounting procedures foreign to the businessman. Other avenues of competition, such as brokerage and promotion, are discouraged by the *per se* nature of the sections of the

77/ 15 U.S.C. § 15; 15 U.S.C. § 12.

statute governing those activities. And the penalties for violation of the Act are out of all proportion to any potential injury which might result from price discrimination.

To be sure, the Act does not compel a finding of liability in every case of price discrimination. A firm charged with a violation may be able to demonstrate lack of competitive injury or the applicability of one of the defenses. 78/ However, evidence before the Review Group and leading Robinson-Patman cases show that this possibility is slight and the risks great. A conscientious attorney must counsel restraint on the basis of numerous cases which impose liability for pricing practices similar to those that a client may be considering. So advised, a rational businessman will find that the risks of selective discounting under Robinson-Patman are severe. The reasonable and necessary consequence of Robinson-Patman's bias must be to create in the business community an atmosphere where caution, not competition, is the rule in setting non-uniform prices.

The biases built into the Act catch the unwary violator, of course, as is demonstrated by a reading of Robinson-Patman case law. But the deterrent effect on wary businessmen contemplating the legality of a price reduction is the real harm, since the pricing practices which give rise to liability under the statute in many cases are those necessary to the proper functioning of the marketplace.

78/ See notes 13 and text at pages 18-27, *supra*.

B. Robinson-Patman Reduces Pricing Flexibility, Discourages the Development of Efficient Distribution Systems and Frequently Operates to the Detriment of Consumers

The previous section of this chapter explains how Robinson-Patman extends the impact of the statute beyond that of protecting competition. The Report will now take a hard look at the problems which Robinson-Patman has caused for businessmen, both large and small, and for the American consumer.

Two seeming difficulties with any discussion of the Act's effects initially must be confronted. The first is the lack of any quantitative study of the overall dollar cost of Robinson-Patman enforcement. The way in which economists and statisticians normally go about determining the cost of a particular statute or other governmental policy is to do a comparative study of business behavior before and after that policy goes into effect, or to perform a "controlled" experiment. A "controlled" experiment is carried out by comparing business behavior in one sector of the economy or region of country where the statute applies with the behavior of firms in a similar market not covered by the law. Studies of this type were conducted to determine the effect, if any, of "Fair Trade" statutes, the enabling legislation for which was recently repealed by Congress. 79/ Valid comparisons of pricing behavior and the survival rate of small businesses could be made since several states had retail price maintenance statutes, several states did not, and several had price maintenance statutes which were later repealed. Similar studies have also been done comparing regulated and unregulated markets in the trucking and domestic airline industries.

79/ Pub. L. No. 94-145, 89 Stat. 801.

With Robinson-Patman, though, such studies are not possible. Robinson-Patman applies throughout the United States and covers the sale of most commodities, including almost all products to be sold to retailers. Moreover, insofar as Robinson-Patman inhibits businessmen from competing for new markets or new customers, the costs of Robinson-Patman are "opportunity costs," that is, the costs to an entrepreneur of having to take the second best alternative because his first choice is blocked by Robinson-Patman. Opportunity costs are inherently difficult to measure.

The second problem is that the actual impact of Robinson-Patman depends on the degree to which Robinson-Patman is obeyed in the business community: to the extent that the statute is ignored, its adverse effects are proportionately reduced; to the extent it is obeyed, its effects are magnified. But again, such data is difficult to obtain. Consequently, it is necessary to assess the economic effects of Robinson-Patman by evaulating the requirements that the statute places on businessmen, by analyzing actual business behavior affected by Robinson-Patman, and by relying on a presumption which all of those involved in the legislative process must make -- that businessmen will for the most part act in the manner logically compelled by a statute and its sanctions. An economist testifying before the Review Group clearly defined the limits of the analytic problem: 80/

> The problem with the Robinson-Patman Act is that it applies all across the country. We simply don't have a country like the United States in every respect except that it does not have the Robinson-Patman Act. If we did, economists would be delighted. We could measure prices in each country and find out

80/ Testimony of Kenneth G. Elzinga, DCRG Hearings, Tr. 261-62.

whether the Robinson-Patman Act in fact has the effects that I am arguing it does. What we are left with, since we do not have the laboratory experiment that we had with Fair Trade, is a much more tentative basis of judgment and logic and inference. I have argued on logical grounds that predatory pricing would be a very rare occurrence as a monopolizing device; it simply doesn't wash from a standpoint of logic. The evidence that has been gathered as to where predatory pricing has allegedly occurred has generally shown that it did not occur or did not have the effects that it was thought to have had. We can look at that type of logic and that type of evidence. Also we are left with the use of inference -- inferring from existing Robinson-Patman Act cases what the effect would be on the market process. . . .

I would like very much to be able to quantify to what extent these prices are raised and that resources are misallocated. I am afraid that that is not perhaps ever going to be possible unless some brilliant economist devises a test that heretofore has not been observed.

The costs to society of Robinson-Patman are both direct and indirect. The direct costs arise from the higher price levels brought about by the Act's inhibitions on the competitive, price-setting process and its encouragement of price-fixing activity. Indirect effects occur when businesses operate less efficiently, pay high legal fees or otherwise incur greater costs because of Robinson-Patman, and when Robinson-Patman places a relatively greater burden on smaller businesses than on large companies.

Following the process of logic and reasonable inference, a witness argued to the Review Group that the probable effect of Robinson-Patman is to raise retail prices in affected sectors by one-half to one percent, plus other losses from inefficiences. 81/ If such a price increase were evidenced in all retail sales, which total around $600 billion, the potential loss caused by Robinson-Patman would be in the neighborhood of $3 to $6 billion. The analysis below shows this to be a not unreasonable estimate.

1. The Act Reinforces Price Rigidity and Stability to the Detriment of Consumers

a. The Act Discourages Pricing Flexibility on The Part of Sellers and Thus Leads to Higher Prices

As shown by analysis of the statute as applied, the key purpose of the Robinson-Patman Act is to prevent the granting of discounts, i.e., lower prices to fewer than all buyers, unless a cost justification or meeting competition defense can be proved. As the preceding analysis has shown it is very easy for a plaintiff to make out a prima facie case, and much more difficult for a defendant to make out any of the defenses. Consequently, the Act serves to mandate extreme pricing caution to the point of inhibiting lower prices -- even those which ultimately would be found not in violation of the Act.

There are several reasons why the filing of private treble damage suits, Federal Trade Commission enforcement actions, or threats thereof would serve to deter price cuts even if the seller believed his action would be lawful and that he would ultimately prevail in a trial.

First, the defendant may reasonably feel that the cost of litigation, even were he to succeed after trial, would be greater than the profits

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81/ Testimony of William F. Baxter, DCRG Hearings, Tr. 53.

which could be made by granting the discount and gaining additional business. Legal services and accounting studies needed to make out a cost justification defense are extremely expensive. Moreover, significant opportunity costs are associated with the delay necessary to evaluate a price-cut decision. A former vice-president of the RCA Corporation explained the predicament: 82/

> Mr. Bennett: Well, the principal problems caused by the requirement of cost justification . . . was the terrible expense. You would have to engage people who are proficient in this work. And they came high. Arthur Anderson and Co. as a company of auditors, for one example. And the work which followed, to establish this cost justification, and in some instances, got to be almost comical to realize the degree that would be invested in trying to find this cost justification.
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> Mr. Flexner: Can you give us an example of the study that you might have engaged to meet the burdens of the test? To see what it cost?
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> Mr. Bennett: Yes; I can give you an example that occurred within our own branches. Started with our Chicago branch but we went a little further than a single independent distributor would go, because we anticipated that once we found some answers that made some sense we would then prevail through the rest of our network of our own branches. And I recall one incident, that was used in the compilation of costs. We were out at a navy pier in Chicago and they ran the elevator up and down with twelve [television] sets on, which would be one sale, versus six sets on, which would be a second sale to another dealer, versus three sets. And, they determined the cost involved in running the elevator. I thought that was a very interesting study.

82/ Testimony of Martin Bennett, DCRG Hearings, Tr. 80-81.

Mr. Flexner: How much did it cost you?

Mr. Bennett: The total study cost us $300,000.

Mr. Flexner: In situations where you would have to do that kind of costing to make a decision about price, were there opportunity risks involved?

Mr. Bennett: Yes. Very frequently, you know, you throw the baby out with the wash water, you go through all this mammoth study, only to find that the condition that caused you to undertake it was no longer existing. That the market place had changed, or whatever reasons, there are many possibilities, and your opportunity was gone because of the time required the effort of many, many people.

The chairman of the American Bar Association Committee on the Robinson-Patman Act testified before the Review Group that it is very difficult for businessmen to compile cost justification data with the certainty ultimately required to prevail in litigation: 83/

The expense and difficulty of cost justification are partly due to the fact that a different type of accounting is involved than is employed in the day-to-day business operations. The collection and allocation of cost data relating to individual customers is not the type of accounting that is done on the current, day-to-day business by companies. It is a method of accounting that, in fact, is unfamiliar to most accountants. Accountants who are called upon to make cost studies in litigated cases usually cannot do so on their own, but have to be guided every step of the way by the legal counsel because of the legal standards that must be complied with as set forth in the Robinson-Patman Act, the decisional law, and task force reports.

Nothing, obviously, can be done to change this as long as cost justification remains a defense under the Act. However, part of the expense and difficulty with cost justification are due to the Federal Trade

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83/ Testimony of Paul H. LaRue, DCRG Hearings, Tr. 206-07.

Commission's insistence on the use of actual costs and on exactness in the calculations which are made. Much of the expense and difficulty of cost justification could be avoided, therefore, if the Commission were to permit the use of reasonable estimates in lieu of actual costs, and be satisfied with a showing of approximate rather than exact cost differences. The uncertainty as to the validity of cost studies, which continues all during a Robinson-Patman Act proceeding until a decision is rendered, is due to the unduly adversary stance adopted by Commission counsel and accountants in many such proceedings. Their strategy in some cases has been to withhold comment and criticism on procedures adopted in the making of a cost study until it was too late to make any substantial changes.

The problem in meeting the cost justification defense is heightened by the fact that businesses often do not make expense records for individual customers, particularly when those customers are small businesses, but only for classes of customers. While it is permissible to give discounts on the basis of class data, it is impossible for a business to know with any degree of assurance whether a class is properly defined and whether a cost justification defense exists for the class. 84/ For that reason a businessman may refrain from offering a discount to a class of small businessmen, even though he believes they deserve it.

Litigation has other direct and indirect costs which deter price reductions believed to be legitimate. Of particular concern to businesses is pre-trial discovery, the legal process by which parties in litigation find out facts under the control of the opposite parties. 85/ Since the key issues in a Robinson-Patman trial involve prices and costs,

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84/ See FTC v. Borden Co., 383 U.S. 637 (1966).

85/ See FED. R. CIV. P. 26-37.

litigants may be able to obtain their competitor's invoices showing prices charged to all customers, the competitor's cost data, and other matters normally considered highly proprietary and confidential. Not surprisingly, therefore, a company faced with possible discovery of competitively sensitive information may decide to forbear from making any selective price reductions or from litigating the merits of any such action upon legal challenge.

Additionally, many corporations, particularly those which are publicly held, desire to avoid litigation. Outstanding major litigation and government challenges must be reported to potential investors under Securities and Exchange Commission regulations. Rather than face presentation of a "blemished" record to the investment community, a company may settle what is really a frivolous suit, or may refrain from making price concessions to avoid such suits when faced with threat of legal action. As one attorney stated to the Review Group: "I think most sellers will do a lot to avoid unnecessary litigation, because many times there is no winner in antitrust litigation. It costs heavily on both sides." 86/

Even if a seller who thinks he has not violated the Robinson-Patman Act is willing to bear the expense of litigation and the notoriety of a suit, he may still refrain from making a price cut because of the fear of the damage consequences of being "unjustly" found to have violated the Act. Under the "automatic damages" rule that has been adopted in some

86/ Testimony of Paul H. LaRue, DCRG Hearings., Tr. 231. See also Testimony of Donald F. Turner, DCRG Hearings, Tr. 313.

circuits, the defendant may be held liable for the absolute difference in price between the favored and disfavored purchasers multiplied by the number of goods sold at the disfavored price. This amount, which is calculated without regard to any real injury suffered by the disfavored purchaser, is trebled, and a "reasonable amount" for attorneys fees is added. The practical difficulty is compounded because in the typical Robinson-Patman case: 87/

> you have a bankrupt small businessman with lots and lots of local creditors bringing the treble damage action against a large remote and wealthy defendant before a jury in a community where the bankruptcy creditor or bankrupt businessman and creditors live. And the prospect of favorable jury verdicts in those cases are very, very small. With the treble damage provision, the threat of such actions is very, very extreme. And I think that it means a great deal of pricing caution by companies even if they are otherwise inclined to compete vigorously.

To the societal costs created by such price inflexibility must be added the cost of administering the Robinson-Patman Act within a business. The former RCA vice-president testified that Robinson-Patman: 88/

> was a constant consideration in our own legal division. And it was constantly being weighed at all of our pricing sessions, when we introduced new products. And I would say there would be 20 or 30 people involved at different periods of time, and try to put an estimate on that, I really couldn't, except, if I may, just say that it was very expensive.

87/ Testimony of William F. Baxter, DCRG Hearings, Tr. 60.

88/ Testimony of Martin Bennett, DCRG Hearings, Tr. 81-81a.

Mr. Flexner: Very expensive?

Mr. Bennett: Yes.

Mr. Flexner: Ultimately, who paid the price of that kind of --

Mr. Bennett: To the extent that all costs of doing business are woven into the cost fabric, the consumer.

A recent court case further exemplifies the anti-consumer effect of Robinson-Patman. The provisions of Robinson-Patman do not apply to sales to non-profit organizations for their "own use." 89/ An association of retail drug stores recently obtained a Supreme Court ruling that refills by a hospital pharmacy of prescriptions given to out-patients did not fall within this "own use" exception. A full hearing will have to be held to determine whether the charging of the lower prices to a hospital pharmacy for that portion of its drugs not dispensed for hospital "use" violated the Act. 90/ If the retail drug stores prevail in their suit, the result most probably will be to raise the prices charged to hospitals for out-patient medicine refills and raise drug company profits -- all to protect retail drug stores from the loss of out-patient drug business to a hospital pharmacy. Since hospital out-patients are often poorer members of society, the effect of Robinson-Patman would be to transfer wealth from the patients most in need of low-cost medical care to the pharamaceutical industry.

In such circumstances, the Act operates exactly as its authors intended it to operate, that is, preventing certain customers from getting

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89/ 15 U.S.C. 13c.

90/ Abbott Laboratories v. Portland Retail Druggists Ass'n, Inc., 425 U.S.1 (19.

lower prices for the manufactured goods they purchase without some "justification." What the authors of Robinson-Patman did not take into account was the fundamental importance of the selective discount as a means to bring down oligopoly prices. 91/

The role of price discrimination in lowering oligopoly prices 92/ may not be obvious at first. By way of introduction, it should be noted that discriminatory prices are likely to exist only where sellers have enough market power to charge some purchasers higher prices than others. For example, one would expect to see discriminations prevail in markets where brand names, patents, or otherwise unique goods give the seller a degree of monopoly pricing power over his product. If, on the other hand, the sellers' market were actually competitive, competitors would rush in to capture the business of those purchasers who were being charged the higher price regardless of the size of the disfavored purchaser. Price discrimination, then, can only exist where there is no seller willing to reduce profit margins to capture the new business of the

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91/ Of course, during the Depression years, Congress sought to raise, not lower, the general price level. See pages 150-53, infra.

92/ An oligopolistic market is one in which there are so few firms that, unlike the truly competitive market, a change in output by one firm will be perceived by the firm as affecting the market-wide price of the commodity. The pricing and output decisions of firms in an oligopoly are thus interdependent. Most such decisions made by a firm in an oligopoly, therefore, take into account the probable reaction of the other firms in the industry. See generally F.M. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE. Ch. 5-10 (1970).

disfavored customer. Adherence to generally prevailing higher prices is just the kind of behavior one would normally expect to see in oligopoly markets.

Both economic theory and observations by attorneys and others indicate that it is the granting of discounts to particular customers with some bargaining power which brings down the high, "sticky" list prices of oligopolistic industries. 93/ Former Assistant Attorney General Donald Turner summarized the importance of price discrimination in achieving the antitrust goal of lowering oligopolistic prices: 94/

> In a truly competitive market, you will never see sellers at the same time selling at a high price and a low price. If there is competition, all of the sellers will move to the high price market and dump supplies in there which would bring that price down and raise the low price. They will go to where they can make the most money.
>
> The very fact that this does not happen indicates that the seller had enough power over the price to keep that high price up, and what is happening is he is forced, unhappily for him, by large buyers' bargaining pressure to drop this price to them.
>
> Now, from an overall economic standpoint, this large buyer bargaining pressure is all to the good. It is a way in which monopoly prices are reduced or oligopoly prices are reduced, and so long as there is adequate competition at the resale level, you can be sure that the benefits obtained by the large buyers in the form of lower prices will be passed on to the ultimate consumer.

93/ See prepared statement of Kenneth Elzinga 23-24, DCRG Hearings; see also the discussion of dynamic pricing, pages 156-58, *infra*.

94/ Testimony of Donald F. Turner, DCRG Hearings, Tr. 308-309.

> So, I say, from a general antitrust perspective and a general economic perspective, the pressures exerted by large buyers are a healthy competitive force and a benefit to the consumer.

Former Assistant Attorney General in charge of the Antitrust Division, Thomas E. Kauper, told the Review Group that monopoly and oligopoly, among other things, produce inflexibly high prices, and that the Robinson-Patman Act, by encouraging price inflexibility, undercuts the basic goals of the antitrust laws: 95/

> I would assume that our concern with single-firm monopoly is in part a concern over that monopoly's prices. It may also, of course, be its general sluggishness in terms of cost innovation -- but surely a major thrust is its pricing activity. And the same is surely true with respect to much of the criticism of concentrated industries. A major concern with respect to concentration, I think, has been the way concentrated industries price. And I recognize you can get into an argument over how they in fact do it, but at least the historical antitrust concern with concentration has been, I think, a price concern . . .
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> I think we, in looking at concentrated industries, look at them in terms of a relatively high degree of pricing inflexibility. Now, one can get violent arguments back and forth about whether concentrated industries add to inflation . . . . But I think if there is anything that is generally true, it is that [their prices] tend to move relatively slowly, that is they are relatively inflexible . . . And that the thing, which based on particular matters we have examined, which seems to be the most disruptive to concentrated industry pricing is discounting. I think that one has only to look over the last three or four months in newspaper accounts, rather persistently given -- as one aluminum company spokesman after another says, "I

95/ Testimony of Thomas E. Kauper, DCRG Hearings, Tr. 333-34.

> don't want to see us get back into the kind of discounting situation we were in a number of years ago."

The reason for an oligopolist's desire to avoid discounting is simple. Where there are few sellers in industry, these sellers recognize that it is to their mutual advantage not to lower their prices across the board. Such sellers can be induced to depart from this course of mutual advantage only by the prospect of obtaining or retaining the business of a particularly wanted customer. Frequently, this desire will require a seller to consider giving selective discounts. A seller is particularly vulnerable to hard bargaining when he believes that the buyer has gotten an offer of a special discount from one of the seller's competitors or that the buyer will produce the product himself by vertically integrating.

Once a price concession is made, it will most likely become known in the industry; other buyers will demand the same concession or, if the demanded concession is not forthcoming, will seek out other suppliers in the oligopoly. Eventually the high list price structure will break down. The Robinson-Patman Act operates to retard or prevent this process: 96/

> Economic theory neatly shows that in an effective cartel, each collusive member has an incentive to "cheat" on the monopoly price and restricted output, by cutting price and producing more than the restricted output. To the extent the cartelist is prevented by

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96/ Prepared Statement of Kenneth G. Elzinga, at 12, DCRG Hearings.

> the antitrust laws from cutting a price to a selected buyer, for fear of the Robinson-Patman Act violation, the cartel has a simpler job of maintaining internal discipline stability, to the benefit of the price-fixers and the detriment of the industry's consumers.

Another economist made similar observations about the importance of countervailing power on the buyer's side in controlling manufacturers' oligopoly prices: 97/

> A limited degree of monopoly ("substantial bargaining power") on one side of the market can be of great service in maintaining competition on the other. A strong, alert, buyer large enough so that the loss of his patronage is not a matter of indifference, constantly on the watch for a break which he can exploit by rolling up the whole price front, able to force concessions first from one and then from all, followed by the other buyers, can collapse a structure of control or keep it from ever coming into existence. Small wonder, as the NRA experience showed, that sellers attempt to keep big buyers out of the market or to restrict their bargaining power. (Footnote omitted)

Empirical confirmation of the role of larger buyers in "policing" oligopoly profits on the seller's side comes from a recent economic study. 98/ That study analyzed margins in 94 manufacturing industries determined to have "substantial market power in the middle 1960's" on the basis of buyer concentration in the market in which they sold their products. The report concluded that the data supports the hypothesis that an oligopolist's ability to exercise market power "is heavily influenced by the structure of the buyers of an industry's products. Furthermore, the interactions between these two elements of industry structure and industry

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97/ Adelman, Effective Competition and the Antitrust Laws, 61 HARV. L. REV. 1290, 1300 (1948).

98/ R. McGuckin & H. Chen, Interactions Between Buyer and Seller Concentration and Industry Price-Cost Margins (Revised) 10, 17, 18 (October 1975) (unpublished).

price cost-margins appear to be significant." Importantly, the role of buyer structure in reducing profit margins may be more significant in the consumer goods industry than in the producer goods sector.

An example of specific instances in which discounts undercut an oligopoly price structure was given by a Review Group witness: 99/

> Now, another thing is that you ought to look at is our merger laws development. The thing that we have been most concerned about is not single firm monopolies, but is a small group of firms dominating the business and practicing what amounts to tacit collusion. They do not have to communicate because they keep an eye on each other. . . . What you are interested in in that kind of situation, Mr. Morris, is that buyers put the heat to these oligopolists to get special deals so that they do not know that everyone is charging the same thing.
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> I worked in private practice . . . on the Electrical Equipment Treble Damage cases. What happened was the utilities would deal around -- which is what led to a conspiracy. Here you have these manufacturers who were basic oligopolists, and they started getting pressed to give special deals, and the next thing you know, the general price was going way down. . . . But it was the fact that the smart buyers could negotiate for special deals and pushed that price structure down (and here led to a conspiracy, which was challenged under the antitrust laws).

In a memorandum to the Attorney General discussing his recommendation to dismiss a pending monopolization action against major tire manufacturers, former Assistant Attorney General Thomas E. Kauper stated that at the time the case was brought, the Antitrust Division did not realize the extent to which

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99/ Testimony of Donald I. Baker, DCRG Hearings at 285-86. Mr. Baker, who is now Assistant Attorney General in charge of the Antitrust Division, was at the time of the DCRG Hearings testifying as a professor of law.

oligopolistic prices could be forced down to near competitive levels through discounting and countervailing buyer pressure: 100/

> When we filed these cases, we focused on the high degree of concentration existing in the tire industry at the manufacturing level. I now believe we did not adequately assess the significance of the industry's retail distribution structure as a possible check on the market power normally associated with such a high level of concentration. In reality, it appears that the countervailing power of large buyers in the final product market, the oil companies and chain stores such as Sears and Montgomery Ward, significantly limit the major tire manufacturers' market power and tend to keep tire prices nearer competitive levels than might be expected considering the level of manufacturing connection. The diversity of retail distribution channels also apparently led to a discount structure that facilitated price cutting.

Significantly, recent antitrust prosecutions suggest that oligopolists have sought to forestall this dynamic discount process by agreement. In testimony before the Review Group former Assistant Attorney General Kauper pointed out that one of the most common forms of price-fixing agreements alleged in antitrust indictments over the last three years has been the agreement not to give discounts. Simply put, such agreements come into existence to eliminate the great uncertainty which leads to price competition in oligopolistic industries. Firms understand that being required to match discounts could result in price reductions which the firm would not

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100/ Memorandum to the Attorney General, dated February 23, 1976, at 5, n. 1 (released March 2, 1976).

otherwise "have to" make. 101/ A recent antitrust case is in point. 102/ Testimony was given at trial that one of several competing bakeries became concerned that industry discounts would cut into its profit margin and persuaded the Federal Trade Commission to commence an investigation into discriminatory pricing in that area. 103/ Further testimony was heard that after the investigation closed without further government action, the bakers agreed to eliminate discounts. 104/

The role of "discriminatory" discounts in oligopolistic industries is demonstrated by a comprehensive Federal Trade Commission report on the structure of the food industry. That report found that "the most pervasive" discriminatory pricing in the food industry occurred in fluid milk, ice cream, and bakery products, industries which are particularly concentrated in localized markets. 105/ The report also indicated that, along with coffee, these same industries evidenced the greatest vertical integration, i.e., food store manufacturing: 106/

> The preceding analysis indicated that food retailers tend to integrate most extensively into the most concentrated food manufacturing

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101/ Testimony of Thomas E. Kauper, DCRG Hearings, Tr. 334-35.

102/ United States v. Cotton, Inc., Cr. 75-43, M. D. La., verdict (August 29, 1975).

103/ The investigation, ironically, was sought to establish that the discriminations would injure competition among the purchasers of bakery products.

104/ Upon trial of the antitrust charge, the defendants argued that the agreements were simply designed to avoid giving discounts which would violate the Robinson-Patman Act. The judge instructed the jury that an agreement to eliminate discounts would not be a violation of the Sherman Act if it was not motivated by a simple desire to raise prices. The defendants were acquitted.

105/ FEDERAL TRADE COMMISSION, ECONOMIC REPORT ON THE STRUCTURE AND COMPETITIVE BEHAVIOR OF THE FOOD INDUSTRY, 186 (1966) [hereinafter cited as 1966 FTC FOOD STUDY].

106/ Id. at 71.

industries. As explained above, concentrated food manufacturing industries tend to have higher profits and larger marketing margins due to heavy promotional expenses than do the less concentrated industries. Hence, these findings support the hypothesis that large retailers integrate into food manufacturing so as to share in these oligopolies and/or to enhance their own profits by eliminating the high costs of achieving product differentiation. (Footnotes omitted)

Again, it is not surprising that this should be the case, since purchasers will have an incentive to go into business themselves to escape oligopoly pricing practices. The important question is whether the oligopolists, once realizing that many of the larger buyers will integrate rather than pay the high oligopoly prices, will offer lower prices to those buyers to avoid losing the customer entirely. Of course, the answer is that the Robinson-Patman Act may prevent the oligopolistic seller from granting the selective discount. Because the oligopolistic seller will almost never lower its price to all of its customers, the large buyer may very well be forced to integrate. This situation helps neither the seller, nor the remaining customers, because the latter might now have to pay that portion of their supplier's overhead which could have been recovered through sales to the larger buyer.

The result is price inflexibility, as the most comprehensive study of the effects of the Robinson-Patman Act concluded: 107/

> There is a consensus of opinion among both buyers and sellers that the result [of Robinson-Patman] has been to diminish the flexibility of prices; indeed, many of the persons interviewed

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107/ C. EDWARDS, THE PRICE DISCRIMINATION LAW 630-31 (1959).

> regard this as the chief virtue of the statute. It is probable that in oligopolistic industries the outlawry of discriminatory concesssions has reduced the principal kind of price competition that still existed under conditions of concentrated production and sale. It is probable that, in an industry that has achieved conspiracy by direct agreement . . . the elimination of unsystematic price cuts has removed the principal weakness of the conspiracy. Proof of neither of these propositions has been obtained during the study; but it was not to be expected that evidence pointing to possible violations of the Sherman Act would have been volunteered by participants in such arrangements. However, the interviews strongly support the inference that the reduced pressure of buyers for concessions and the enhanced risk of the seller who makes concessions have tended to make sticky prices stickier and thus to reduce the flexibility and responsiveness of the price system. The effect has been great enough to be prominent in the thinking of businessmen who like it as well as businessmen who do not like it.

Some proponents of Robinson-Patman have stated that requiring price changes to be uniform actually helps lower prices in oligopolistic industries. This is so, it is argued, because when a large buyer negotiates with his supplier -- and this will be through lawyers rather than businessmen -- the buyer will "require" that the seller lower his prices uniformly, thus giving the smaller purchasers an unexpected break.108/ But the Edwards' study found that one effect of the statute was that "price change tends to take place only where the pressures toward it are great enough to justify an upward or downward movement of the entire price structure." 109/ It is highly unlikely that in most industries there will exist a buyer so powerful that it can force down the price levels in the industry as a whole.

108/ Testimony of Jerrold C. Van Cise, 1976 House Hearings, Tr. 159-60.

109/ EDWARDS, supra note 107, at 630.

Indeed, if such a buyer does exist, the fact of his power bodes ill for that firm's smaller competitors, who would seem to be in deep trouble with or without Robinson-Patman. In most industries, as former Assistant Attorney General Kauper noted, list prices will remain "sticky" and if Robinson-Patman makes a price cut an all-or-nothing affair, in most oligopolies, the answer will surely be "none." As one witness put it: "One could describe the Robinson-Patman Act as a form of fair trade legislation at the manufacturer level because that is exactly what its major thrust is."110/

Federal Trade Commission orders enforcing the Robinson-Patman Act may also serve to increase industry pricing inflexibility by decreasing the likelihood that discounts will be granted. According to a former FTC Commissioner, the FTC had asked executives of companies subject to Robinson-Patman order to describe the effect these orders had on their companies, a survey taken in conjunction with the Brooks' Report, p. 238, infra: 111/

> Some of the comments we received were very revealing. One of them, for example, gave this summary of his experience with our orders in this area; "there is less vigor," he told us, "in competitive pricing now. Prices are "more set" than before the [FTC] ruling. . . . We don't have to football as much as before, therefore [it is] an advantage to us." Another commentator explained: "It is probable that the final furniture prices by suppliers affected by FTC action to IFB's clients would have been

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110/ Testimony of William K. Jones, DCRG Hearings, Tr. 32.

111/ Statement of Mayo J. Thompson, Hearings Before the Joint Economic Committee, November 18, 1974 at 7.

lower by 10 to 20 percent without the FTC decision.

Finally, Robinson-Patman has one other effect on pricing which has only recently come to the fore as a problem. By requiring uniform prices to most purchasers, and permitting discounts only where they are cost justified, the Act inherently tends to establish a "cost plus" criterion as the pricing norm. Consequently, businessmen become more interested in pricing on the basis of cost rather than in responding to changes in demand. 112/ Experience with the recent inflation suggests that many corporations now seem to price solely to recover their costs rather than in response to demand conditions. Thus, businessmen may tend to raise their prices even in the time of fallen demand, an approach that in great part may stem from the cost justification provisions of recent wage and price controls. This phenomenon has caused much concern with respect to the ability of our economy to respond to macroeconomic policies. To the extent Robinson-Patman may encourage the continuation of this type of pricing practice after the demise of controls, the Act stands in contradiction to the vital goal of bringing inflation under control.

b. Robinson-Patman Act Encourages Exchanges of Data Among Competitors and Price Fixing

A fundamental premise of the antitrust laws is that businessmen must make independent decisions about price if the free market system is to work properly. For that reason courts have interpreted the Sherman Act to ban any price agreement. Similarly, exchanges of price information which tend to produce uniform or coordinated pricing among competitors have been

112/ P. KOTLER, MARKETING MANAGEMENT 78 (1972).

declared unlawful. The Robinson-Patman Act by serving as an excuse for and encouragement of price fixing confounds this fundamental antitrust policy.

Avoidance of Robinson-Patmam liability under the meeting competition defense requires a showing that the price differential was necessary to meet a lower price offered by a competitor. The seller wishing to use this defense must also show that he made "reasonable efforts" to learn whether in fact the lower price reported by the buyer had actually been offered by a competing seller. While the Act, as interpreted, does not require that these efforts include checking the price quote directly with the competitor, some have contended, on the basis of court decisions, 113/ that dicussions of price quotes among competitors which would otherwise violate the Sherman Act may be justifiable when done in compliance with the Robinson-Patman Act. That Robinson-Patman is increasingly becoming a cover for hard core price-fixing agreements was confirmed by former Assistant Attorney General Kauper before the Review Group. Mr. Kauper stated that on several occasions attorneys representing companies under investigation for price fixing argued that any discussion of prices was motivated by the need to comply with the meeting competition defense. The argument would also be made that agreements to eliminate discounts illegal under Robinson-Patman should not be prosecuted.

Mr. Kauper conceded that some of these price discussions would have taken place without Robinson-Patman. However, the former Assistant Attorney General

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113/ E.g., Belliston v. Texaco, Inc., 455 F.2d 175 (10th Cir. 1972), cert. denied, 408 U.S. 928 (1972). This issue is on appeal in United States v. United States Gypsum Co., Cr. 73-347, W.D.Pa., verdict July 15, 1975, appeal pending.

has concluded that the potential Robinson-Patman justification implicit in the meeting competition requirements encourages the exchange of price information, and that this exchange clearly promotes price stabilizing agreements: 114/

> Now I don't think it is a deep dark secret that there are buyers in the market who are known to misrepresent what the price offering they have received from a competing seller is. Certainly there are many major sellers who believe that is the case -- and, therefore, that the only reliable way to find out what that competitor is charging is, one way or another, to inquire directly of him.
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> And thus you find in some industries relatively extensive exchanges of price information for the purpose, at least the stated purpose, of complying with the Robinson-Patman Act. Now, it is certainly true that in some cases that may be nothing more than after-the-fact rationale, but I suspect there are a good many cases in which that is done in good faith.
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> Now, the mere exchange of price information itself may tend to stabilize prices. But I think it is also relatively common that once that exchange process begins, certain understandings go along with it -- that we will exchange prices, but it will be understood, for example, you will not undercut my prices.
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> And from there it is a rather easy step into a full-fledged price-fixing agreement. I think we have seen that from time to time, and I suspect we will continue to see it as long as there continues to be a need to justify particular price discriminations in the terms of the Robinson-Patman Act.

114/ Testimony of Thomas E. Kauper, DCRG Hearings, Tr. 336-37.

> Now, whether one would conclude that there would be no price fixing, if there were no Robinson-Patman Act, in those precise industries, in those precise periods of time, is obviously an impossible question to answer. But I think it is true that a pattern of communication back and forth tends to lend itself relatively easily to taking the next step, which is simple agreement among them not to compete, or not to give discounts, or not to give discounts at a particularized level.

The use of Robinson-Patman as a justification for price discussions alleged as part of price-fixing conspiracy is exemplified by the recent Gypsum prosecution in Pittsburgh. 115/ In that case, the defendants, major manufacturers of gypsum wall board, were convicted by a jury of price fixing in violation of the Sherman Act. The former chief prosecutor for the Antitrust Division testified before the Review Group that the defendants in that case sought to justify the conspiracy on the basis of Robinson-Patman compliance. 116/

Looking beyond the Gypsum case, the former chief prosecutor observed that "[i]ntercommunication on competitive matters is also facilitated considerably by this facade, this sham, of alleged compliance with the Robinson-Patman Act." 117/ He also explained how the exchange of data tends to keep prices at a stablized level even without an express price fixing conspiracy. When a customer claims he has received a lower price, the supplier may call his competitor to learn whether that price quote was actually given. If it is believed that the claimed discount had not been given then the original seller will, of course, not lower his price. Where, on the other

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115/ United States v. United States Gypsum Co., Cr. 73-347, W.D. Pa., verdict July 15, 1975, appeal pending.

116/ Testimony of John Fricano, DCRG Hearings, Tr. 65.

117/ Id., at Tr. 68.

hand, the competitor confirms the offer of a lower price, the seller need only meet that price. Without such confirmation, the seller would be forced to rely on his buyer or to guess at the actual price offered by the competitor. Under these circumstances, the seller might, in the short run, offer lower prices than necessary to meet the competition. Thus, lack of communication would create uncertainty on the part of a seller when faced with the claim that a competitor is charging a lower price; this uncertainty would very likely lead to the outbreak of true price competition and a lower price to the consumer.

In the regional bread price fixing case referenced above,118/ defendants were acquitted after the court heard testimony relating to the existence of an actual agreement to fix prices, and also testimony that any agreement, if it existed, was simply for the purpose of eliminating discounts which would have violated the Robinson-Patman Act. Again, it is not possible to state whether the defendants' price-fixing agreement would have existed without the Robinson-Patman defense, but this was the defense used and the defendants were acquitted by the jury.

In his testimony before the Review Group, the Gypsum prosecutor said that on the basis of his experience in that and other cases, he has concluded that the Sherman Act and Robinson-Patman are antithetical statutes: 119/

> There is no reconciling the Robinson-Patman Act and the Sherman Act. With regard to

118/ See text at note 102 , supra.

119/ Testimony of John Fricano, DCRG Hearings, Tr. 69. See also Levi, The Robinson-Patman Act--Is it in the Public Interest? 1 ABA ANTITRUST SECTION REP. 60, 62 (1952).

competition, I would take it a step farther. I think the Robinson-Patman Act just doesn't fit into our capitalistic free enterprise system whatsoever.

c. Under Robinson-Patman, Buyers Are Encouraged to Negotiate for Price Reductions With Undue Restraint

Section 2(f) of the Robinson-Patman Act makes it unlawful for a buyer to knowingly induce or receive a discriminatory price which would violate Section 2(a). Thus, the buyer is exposed to risk of litigation and substantial treble damage losses.

While this provision was intended to counteract the power of large buyers to "coerce" non-justified price discriminations from smaller sellers its applicability is general and therefore is restrictive in situations where vigorous bargaining by a buyer is necessary to bring down high prices charged by large oligopolistic manufacturers.

It is anomalous that a statute designed to protect small businessmen has the effect of governing the competitive relationships between giant companies for the benefit of those with oligopoly selling power. The conflict between the Act's goal and its result is evidenced by a case involving a dispute between the Kroger food chain and the Beatrice Foods Co., one of the largest dairy processors in the industry. In that case the Federal Trade Commission found that Kroger violated Robinson-Patman as a buyer when it misrepresented to Beatrice the size of discounts it was getting from other dairies, thereby inducing Beatrice to discriminate in price. 120/ In a recent case, 121/ however, the FTC recognized that

120/ Kroger Co. v. FTC, 438 F.2d 372 (6th Cir. 1969), *cert. denied.*, 404 U.S. 971 (1971).

121/ The Great Atlantic & Pacific Tea Co., Inc., [1973-1976 Transfer Binder] CCH TRADE REG. REP. ¶ 21,150 (FTC 1976).

such a policy might undercut the vitality of the bargaining process. It therefore refused to require a seller to disclose that an offered price was below that necessary to meet that of a competitor. Any other outcome, the Commission noted, would serve to make a mockery of the antitrust goal of preserving hard bargaining to bring down non-competitive prices. Constraining a buyer's ability to bargain by imposing an affirmative duty of disclosure simply frustrates the negotiation process: 122/

> [Neither the buyer nor the seller in price negotiations] expects...or can be expected, to lay all his cards face up on the table. Battle of wits is the rule. Haggling has ever been the way in the market place.

d. Robinson-Patman Restricts Competition For New Markets and Customers

It is a fact of business life that over time an inertia builds up in the buying habits of customers. Whether because people generally feel more comfortable operating out of habit, because consumers have learned the quality of a product marketed under a brand name, or because a businessman believes a steady supplier will serve him more effectively, purchasers are reluctant to switch sellers absent the promise of compelling

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122/ *Id.* at 21,040, citing Forster Mfg. Co. v. FTC., 335 F.2d 47, 56 (1st Cir. 1964), *cert. denied*, 380 U.S. 906 (1965).

benefit from the change. While the possibility that a new supplier will provide a better product or better service plays a rôle in a decision to switch suppliers, a more important reason is the ability of a new supplier to offer a commodity at a lower price. The necessity for a competitor seeking a new customer to offer a price advantage will be all the greater if the current seller is a firm of established reputation, and the prospective seller is a relative newcomer to the area or new entrant to the industry.

The ability of firms to enter new markets is, of course, a key to keeping such markets competitve. Particularly in local or regional markets where the number of competitors is relatively small, the most effective deterrent to the establishment of collusive or oligopolistically high prices and profits margins is the likelihood that these conditions will attract new business into the area. Hence, unless some sort of barrier to entry is erected around a local monopoly or oligopoly, entry or the threat of entry will serve to constrain the power of entrenched firms to charge monopoly prices. As will be shown, Robinson-Patman serves as such a barrier because it discourages firms from undertaking a promotional pricing campaign in connection with an attempt to enter a new market, unless that campaign is conducted on a nationwide basis or reflects some special cost saving of serving that market. Such foreclosure of potential competition is directly contrary to antitrust purposes embodied in Section 7 of the Clayton Act. 123/

123/ *See* United States v. Penn-Olin Chemical Co., 378 U.S. 158 (1964).

In many sectors of the economy, the most likely source of new entry is from firms already selling a commodity in other areas. As one economist described the importance of geographical expansion to entry:124/

> Basically there are only two ways [to enter a market]: a new enterprise is begun and sells its product in the oligopolized territories; or an existing firm located outside the territory enters. The new firm could either start in the territory or ship into it from outside facilities. The existing firm, in like fashion, could either ship into the territory in question or build an affiliate there.
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> *De novo* entry is certainly not unheard of in this country. With apparently unflagging optimism, the U.S. economy generates brand new business firms. But for many domestic markets, the principal entry threat is from the established firm producing the identical or similar product in an other part of the country. For example, in the brewing industry, there has been no successful new entrant in recent years; but a healthy pro-competitive force has been the expansion into larger marketing territories of a number of the regional brewers.

The first way in which Robinson-Patman erects entry barriers is through Section 2(a)'s prohibition of primary line price discrimination. The leading case here is *Utah Pie*.125/ In that case, a local pie manufacturer had a 66% share of the frozen pie market. Several national pie

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124/ Prepared Statement of Kenneth G. Elzinga at 16, *DCRG Hearings*.

125/ Utah Pie Co. v. Continental Baking Co., 386 U.S. 685 (1967). See text at pages 15-17, *supra*.

manufacturers sought to enter this market by charging prices which were lower than those charged by them in neighboring states, but were not clearly below the variable costs of each price cutting firm. Vigorous cost competition broke out; yet at all times, the local firm, Utah Pie, remained profitable. Moreover, at the end of the period of "discrimination" Utah Pie remained dominant in the market with a 45% share. The Supreme Court also found that the frozen pie market in Salt Lake City was highly competitive, that Utah Pie was at times the leader in moving prices down and that the defendants were the leader at other times.

On these facts, the Court concluded: 126/

> We believe that the act reaches price discrimination that erodes competition as much as it does price discrimination that is intended to have immediate destructive impact. In this case, the evidence shows a drastically declining price structure which the jury could rationally attribute to continued or sporadic price discrimination.

Under the Robinson-Patman Act, as interpreted by the Supreme Court, a declining price structure could be the basis for a jury finding that the price cuts met the statute's test of potential harm to competition. Similarly, under the Act, Utah Pie's dominance was viewed by the Court as irrelevant: "Nor does the fact that a local competitor has a major share of the market make him fair game for discriminatory price cutting free of Robinson-Patman Act proscriptions."127/ Finally, under Robinson-Patman evidence of "predatory intent" could be inferred from the fact that the

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126/ 386 U.S. at 703 (emphasis added).

127/ Id., at 703 n. 14.

selling price in the Utah market was less than direct cost plus an allowance for general corporate overhead. 128/

One economist speaking before a congressional committee felt that the result in Utah Pie was justifiable because the Utah Pie Co. was a small business and national firms should not be given the opportunity to use discriminatory pricing to impinge upon the ability of the local company to maintain good profits. 129/ The most important result of this case, however, was not the actual resolution of the dispute between Utah Pie and its competitors, but the rules of competitive restraint which the Court established under Robinson-Patman for all geographic pricing patterns in the United States. Thus a leading antitrust attorney testified before the same congressional committee that a major effect of the case was to establish as precedent the conditions under which firms would be subject to treble damage liability.

The irony of the Utah Pie precedent is that it rests on facts normally associated with healthy, non-injurious competition: 130/

> Far from being injured, the plaintiff remained the leader in the market, met and even undercut the defendants' prices, increased its sales, and operated profitably. Consumers benefited from the lower prices

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128/ Id., at 698.

129/ Testimony of Robert Brooks, Subcommittee Hearings, pt. 1 at 426-30.

130/ Prepared Statement of Paul H. LaRue, Subcommittee Hearings, pt. 2 at 227.

> of frozen pies and greatly increased their purchases of all brands in the market.

Most businessmen will desire to enter a market if they can cover their marginal costs of doing business there. Such behavior may well be discouraged by the Supreme Court's ruling in Utah Pie that predatory intent could be inferred from pricing in a regional market below the fully allocated costs of doing business there. Moreover: 131/

> The Court's statement that, even apart from the evidence of predation, the jury's injury finding was justified by the evidence of "a drastically declining price structure," contains a faulty standard of competitive injury. A declining price structure in a market of numerous sellers signifies not a lessening but an intensification of competition. And if the claimed victim of price discrimination continues to realize a profit when prices are their lowest, as did Utah Pie, what basis is there for a finding a competitive injury? Clearly, the Court fashioned an anticompetitive standard which flies in the face of Sherman Act policy favoring vigorous price competition.

Insofar as manufacturers pay heed to the teachings of Utah Pie, they may be reluctant to engage in promotional pricing to enter a new area: 132/

> A legal standard such as this renders every regional or local price reduction or promotion by a large seller a potential Robinson-Patman violation. It is also the despair of lawyers who counsel such sellers on compliance with the Act, since they can never give assurance that the sellers' proposed price reductions or promotions will not violate the Act if there is a chance that competitors will meet them and bring down the market price.

131/ Id.

132/ Id. at 228.

If the inability to undercut the price of entrenched firms prevents outside firms from overcoming buyer inertia, and from gaining a sufficient customer toe-hold in the new market, then the local oligopolists will remain secure in their positions and local consumers will have to pay higher prices. The benefits of new entry were demonstrated by a Review Group witness: 133/

> I represented in private practice years ago a local monopoly seller of an . . . exotic food product. A big national manufacturer came in and started giving one free for two and that sort of thing, and my client's market share went from 85 percent down to 45 percent.
>
> What did he do? He got rid of his not-so-good advertising agency, fired several inefficient employees, and got out and hustled. As far as I know, he is still doing very well, but he does not have 85 percent. It was the spur of the outside that was important.

The next way the Act adversely affects entry is through its application to secondary line situations. Testimony before the Review Group indicated that the smaller buyers may threaten suit to prevent suppliers from granting price concessions to larger purchasers. A supplier faced with this situation must give up the ability to meet the price specifications of larger buyers, grant the price cuts, and face potential treble damage liability, or incur the massive loss of a universal price reduction. The Review Group heard testimony that, in fact, in one such situation a larger supplier of an important consumer good withdrew entirely from a major metropolitan area because of threatened Robinson-Patman litigation on one side and buyer demands on the other. 134/

133/ Testimony of Donald I. Baker, DCRG Hearings, at 285.

134/ Testimony of Christian L. Campbell, DCRG Hearings, Tr. 142-143.

The secondary line provisions of Robinson-Patman also severely inhibit the ability of suppliers to compete for the business of new purchasers, where the goods sold will eventually be resold by competitors of the potential customers. Because of the difficulty of knowing whether a particular discount will satisfy the cost justification defense, a seller may be hesitant to make a price concession without spending some time in checking out the costs of the transaction. By the time this is done, the competitive opportunity may be lost as the new purchaser will have obtained his goods from someone else who is able to quickly offer a lower price. Testimony was heard before the Review Group that, in fact, a television distributor had lost a sale opportunity because it could not quickly determine whether it could offer the purchaser a price competitive with that of other television manufacturers. 135/

More importantly, the meeting competition defense only permits a supplier to "meet, but not beat" the price quote of a competitor. 136/ As noted, it is difficult to overcome established trade relationships unless the seller can offer a better price than his competitor. Insofar as a seller is not able to undercut the price that a purchaser is getting from another supplier, he may not be able to get new business in sufficient quantity to remain in the market. 137/

135/ Testimony of Martin Bennett, DCRG Hearings, Tr. 81.

136/ See text at page 25 , supra.

137/ Moreover, it was not until 25 years after the passage of Robinson-Patman that courts permitted businesses to use the meeting competition defense "offensively" in order to gain new business. Prior to that time, a businessman could only use the meeting competition defense to retain customers. Even after such court decisions, the FTC announced that it would continue to rely on earlier court decisions barring such offensive use. See text at p. 26 supra.

In the real world, it is often difficult for a businessman to know whether he will be able to make use of the meeting competition defense at all. A manufacturer or a wholesaler is not entirely free to rely on his customer to tell him what price he must meet. Courts and the Federal Trade Commission usually do not permit a seller to meet the "good faith" requirement of the defense merely by relying on the say-so of his customer. 138/ He must make other reasonable efforts to satisfy himself that the other offer has in fact been made. The difficulties were described by a former RCA executive: 139/

> Mr. Flexner: Could you describe some of the problems that your distributors would confront in trying to deal with the meeting competition defense?
>
> Mr. Bennett: Well, you start out with a simple premise of what is the competition in reality, out in the real world. What's it doing? Now, your first information comes naturally in the form of a conversation from the dealer to the distributor. And I'm not questioning the dealer, he, the distributor, had him as a customer for many years, and you hope to have him continue as a customer, and so you must take his word. But that, of course, is much too vague for [a] reason to meet the competition. So the problem is to get some factual materials, such as the ultimate, getting a copy of the invoice of the competition, describing the price, for reasonably similar goods.
>
> Mr. Flexner: Is that an easy thing to do?
>
> Mr. Bennett: No.

138/ See e.g., FTC v. A.E. Staley Mfg. Co., 324 U.S. 746, 759-60 (1945).

139/ Testimony of Martin Bennett, DCRG Hearings, Tr. 78-79.

> Mr. Flexner: In situations where that can't be done, has it been your experience that because of the risk of Robinson-Patman and the uncertainty of meeting the competition the distributor would exhibit extreme caution in terms of trying to compete?
>
> Mr. Bennett: Yes, very definitely. Caution was definitely the watch word in the pricing area of all goods.

Of course, if the corroboratory evidence were not available, a seller's legal counsel might advise him against making an offer to meet the reported "lower price."

Consequently, in secondary line cases, as in the primary line cases, when there is doubt as to the legality of a price intended to meet competition, the businessman must lower prices for all his sales among competing purchasers. It is a simple matter of fact that most firms do not have the financial basis to lower their prices to all customers in order to gain the business of a few of them. As a practical consequence of these restrictions, such efforts to gain new business may not be made.

Even the restrictions contained in Section 2(d) of the Act requiring promotional allowances to be paid only on a "proportional" basis have served to inhibit entry. One attorney testified before the Review Group that one of his clients wished to enter a market then dominated by a monopolist by the only practical way, that is, by offering large promotional allowances to the largest distributor in the market. Indeed, the key distributor demanded a greater promotional allowance than the current dominant firm was paying. Since the client could not afford to make the promotional allowance available on a proportional basis to all the distributors in the market as required by the Robinson-Patman Act, the firm decided not to enter the market. The prospective entrant, had it been able to enter, would have charged a lower price than the monopolist was charging and would, the firm believed, still have been able to make a profit. But in spite of profit potential, the firm simply did not want to run the risk of lengthy Robinson-Patman litigation. 140/ The result of Robinson-Patman, in that case, was to protect the monopolist from new entry.

140/ Testimony of Christian L. Campbell, DCRG Hearings, Tr. 142-44.

2. <u>The Act Fosters Inefficient And Costly Distribution Patterns Often to The Detriment of Consumers and Small Businessmen</u>

a. <u>Robinson-Patman Encourages Proliferation of Private Brands and Product Differentiation</u>

The various restrictions on pricing flexibility give rise to another problem: firms devise costly marketing strategies to avoid legally the Act's prohibitions. Such avoidance tactics arise in two circumstances. First, <u>buyers</u> may believe that the purchase price for a commodity is too high; because the sellers' market is oligopolistic and prices are non-competitive, buyers would like a lower price. Similarly, buyers may not wish to pay for the "use" of the brand name under which the product is sold or for the advertising expense necessary to support it. Second, <u>sellers</u> may wish to expand their sales by offering their products at lower prices to some customers.

In both cases, the manufacturer might find that the simplest way to meet the demands of a customer with bargaining power or to realize his own desire to expand output, would be to lower the price to some customers,141/ but not to all -- a universal price reduction being too costly for the seller. Of course, Robinson-Patman prohibits just such selective reductions. The buyer and seller, therefore, may find it to their mutual advantage to work around Robinson-Patman, the buyer so as to get a lower price, the seller in order to gain or retain the customer.

141/ The seller would probably like to grant the request of the buyer without requiring the buyer to "shop around" for a low price which the seller then can lawfully meet.

The two most readily utilized ways to avoid the requirement of pricing uniformity are private labels and unique product specifications. Private brands are products sold under the seller's rather than the manufacturer's label. Unique specification items are products, such as appliances, which have some small physical difference from the product usually sold by the manufacturer. 142/

The use of artificially differentiated products to avoid Robinson-Patman increases the cost of doing business. Production techniques must be adjusted to manufacture goods of different specification. Inventory and distribution costs are also increased as manufacturers keep separate inventories of goods for each of their important customers, rather than a single inventory of identical items. The parties will nevertheless incur these costs when additional revenue that can be obtained from increased sales outweighs the additional costs.

Private brands effectively escape Robinson-Patman scrutiny even though physically identical products are considered of "like grade and quality" if packaged under a different name. Courts have recognized that because customers are willing to pay a relatively higher price for brand name goods than for so-called private label goods, there is no "injury to competition" under the Act if the private label good is sold at a price set just enough below the price branded good to take into consideration the consumer preference for the brand name. 143/ While

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142/ These techniques may also be utilized to achieve other marketing objectives which are dependent on the sale of essentially the same product at different prices. Thus, even without Robinson-Patman, these techniques would be utilized, but to a lesser extent.

143/ FTC v. Borden Co., 383 U.S. 637, 645-46 (1966).

the opportunity to purchase goods under private labels must be available to all purchasers on proportional terms, in general, only the larger purchasers have the volume and reputation to take advantage of such an offer. Thus, purchasers and sellers may find private labels an effective method of overcoming the inability of the seller to discount the branded item.

It is worth noting that one side effect of Robinson-Patman may be to increase the relative price that poorer persons have to pay for goods compared to that paid by more educated middle-class consumers. As one witness put it, the educated middle-class consumers, aware of the cost savings associated with private label products, can "get around the Robinson-Patman Act", while lower income consumers tend to purchase higher priced nationally advertised brands. 144/

If it were not for Robinson-Patman, there would likely be greater competition in the pricing of brand-name goods and poorer shoppers would be getting prices for the brand-name items that were closer to those which are only available for private label items.

The Act's limited applicability to discrimination in the sales of goods of "like grade and quality" leads to the strategy of ordering commodities that are of somewhat different specification. These goods nevertheless remain in competition, as far as the consumer is concerned, with the standardized model generally sold by a manufacturer. Thus, in a case involving bathroom fixtures, the

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144/ Testimony of Donald I. Baker, DCRG Hearings, Tr. 288-89.

Commission was upheld in its findings that non-functional differences in products made for general distribution and those sold as privately labeled items to Sears, Roebuck and other large purchasers were not of like grade and quality. 145/ Taking advantage of the fact that a relatively minor physical difference can remove the product from the coverage of Robinson-Patman, at least one manufacturer of consumer goods asked its customers to "build their own" product from a parts list in the hopes that the product sold to each customer would be slightly different. 146/ Likewise, in the television industry, a manufacturer may produce a "variation model" which merely involves the cosmetic change of moving the control knob from the front to the side. This permits pricing the variation model at different levels than the standard television in order to accomplish several objectives including the avoidance

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145/ Universal Rundle Corp. [1963-1965 Transfer Binder] CCH TRADE REG. REP. ¶ 16,948 [FTC 1964], aff'd 387 U.S. 244 (1967).

146/ Speech of Jonathan C. Rose before the Legal Affairs Committee of the Grocery Manufacturers Ass'n, October 29, 1975, at 12.

of Robinson-Patman. 147/

When large retailers purchase products under long-term supply contracts, specifications are frequently varied to insure that there will be no Robinson-Patman difficulties. A Review Group witness described the process and its costs: 148/

> If the manufacturer regularly manufactures products one, two, three and four, to sell to retailers in spot markets, then under the supply contract he manufacturers one and a halfs, two and a halfs, three and a halfs, and four and a halfs.
>
> I don't mean to suggest that the product variations are artificial differences; there are real differences. The real differences are built into the specification of these products to make sure that they are not of like grade and quality.
>
> And they succeed in getting this of not like grade and quality. But the consequences are to multiply the number of different products being manufactured, and to deny the economy the advantage of longer production runs on a smaller set of products, which would be more efficient. And the costs to everyone are effectively increased.

b. Robinson-Patman Preserves Inefficiencies in the Distribution Network

Robinson-Patman increases the cost of doing business by adding to the complexities of distribution. To some extent, this result was intended by the authors of the statute: certain classes of distributors were to have a protected status. Other effects, such as prevention of greater efficiencies in distribution and of cost saving backhauls in transportation were not foreseen at the time Robinson-Patman

147/ Testimony of Martin Bennett, DCRG Hearings, Tr. 82-83.

148/ Testimony of William F. Baxter, DCRG Hearings, Tr. 50.

became law. All of these, though, are costly developments which might not have occurred in the absence of Robinson-Patman.

(i) Protection of Brokers

Section 2(c) prevents the paying of a discount "in lieu of" brokerage, or the paying of any brokerage allowance by a seller to a broker who is also the broker of the buyer. This provision, which first appeared in the NRA Code of Fair Competition for the wholesale fresh fruit and vegetable distribution industry, 149/ was justified on the grounds that it prevented "double dealing" brokers from receiving payments from both buyers and sellers, and prevented devious sellers from granting price discounts disguised as payments for "phantom brokerage." A violation of Section 2(c) is a *per se* offense in that no impact on competition need be shown and no defenses are permitted. Thus, the section sweeps far more broadly than do the general prohibitions against discrimination contained in Section 2(a).

While Section 2(c) was specifically directed at the buying practices of the larger chains, such as A&P, the section has served to interfere with and complicate the distribution of goods by independent grocers who have organized in cooperatives. The section has been held to ban brokerage payments to a cooperative brokerage service of independent food stores -- this arrangement, of

149/ Fulda, The Per Se Provisions of the Robinson-Patman Act, 49 TEX. L. REV. 961, 963 (1971).

course, having been established to counteract the buying power of larger chains -- but to permit the establishment of a cooperative wholesale warehouse that actually took title to the merchandise rather than acted solely as agent. 150/ The Act thus requires coop members either to utilize an independent broker or to take collective financial responsibility for the purchases of each member. Such artificial restrictions on coops only serve to reduce the ability of independents to compete with chains.

More importantly, the Act has reduced the ability of purchasers to buy directly from manufacturers who also use brokers. If a manufacturer uses brokers, any discount to a direct-ship buyer may be considered a discount "in lieu of brokerage" and a *per se* violation of Section 2(c) without a showing of competitive harm. Hence, manufacturers may be reluctant to grant any discounts to such a buyer even though by operating on a direct-ship basis, both buyer and seller may operate more efficiently and be willing to pass these savings on to the consumer. Thus, suppliers may be under pressure to eliminate all brokers so that discounts may be given to larger purchasers who would not need brokerage. 151/ On the other hand, the supplier who wishes to use brokers for some of its customers is compelled to use brokers for all. In those cases where businessmen pay for

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150/ Compare Modern Marketing Services v. FTC, 149 F.2d 970 (7th Cir. 1948) with Central Retailer-Owned Groceries v. FTC, 319 F.2d 410 (7th Cir. 1963).

151/ Such a practice was an allegation in the 1943 Antitrust Division Sherman Act complaint against A&P. See EDWARDS, *supra* note 107, at 109.

brokerage service which they do not really want to receive, the result will be inefficiency: businessmen may ask for more services than they need or order smaller quantities more frequently "since they are not free to obtain price concessions even where cost justified." 152/

The inhibitions and distorting effects of Section 2(c) are heightened by the large percentage of FTC resources that have historically been devoted to enforcing the brokerage provisions. Statistics indicate that for the period dating from the time of Robinson-Patman's passage to 1969, of the 439 final orders entered under the Robinson-Patman Act, 180 of them concerned the brokerage provision. 153/ Perhaps this concerted attention reflects the ease of prosecuting a case which does not require proof of injury to competition.

The Attorney General's committee to study the Antitrust laws concluded in 1955 that Section 2(c) was inconsistent with antitrust policy: 154/

> The Committee considers the prevailing interpretations of the "brokerage" clause at odds with broader antitrust objectives. Goods are sped to the consumer through marketing functions, whether performed by independent "brokers" or other businessmen who have invested capital and services in the "middleman" phase of the marketing process. A Legal

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152/ Id. at 151.

153/ Fulda, supra note 149, at 962.

154/ REPORT OF THE ATTORNEY GENERAL'S NATIONAL COMMITTEE TO STUDY THE ANTITRUST LAWS, 190-91 (1955).

disqualification of all but the "pure" broker's distributive services is thus at variance with business realities. Moreover, the essence of antitrust policy in distribution is to assure that the consumer benefits by vigorous competition along each step of the way. Yet the "brokerage" clause as presently interpreted enacts a preferred position for the "independent" broker, thus discriminating against competing firms in distribution who are arbitrarily denied compensation for genuine market functions which they perform. . . . In our opinion, the virtual legal monopoly conferred by Section 2(c) on one type of middleman clogs competition in the channels of distribution, and exacts tribute from the consumer for the benefit of a special business class.

An example of the "tribute" that Section 2(c) exacts from the consumer is dramatically illustrated in a dissent by former FTC Commissioner Elman to a Commission vote to file a brokerage complaint. In that case a seller of lettuce, rather than the buyer, had paid the buyer's brokerage commission. Elman discussed the reasoning of the FTC majority in deciding to file the complaint: 155/

They agreed that if their economic analysis was sound, lettuce prices would be increased but they argued that "such factors should [not] determine whether the Commission enforces" Section 2(c) because, they said, the Commission should not be concerned about the interim allocation of resources among growers, distributors, and consumers. That there was no competitive injury from these practices they also deemed irrelevant, since Section 2(c) "makes no reference to competitive injury." In their view, "the statutory scheme is plain" and it would "frustrate the legislative intent" for the Commission not to issue this complaint. Although it was recognized that "of course, an increase in cost of

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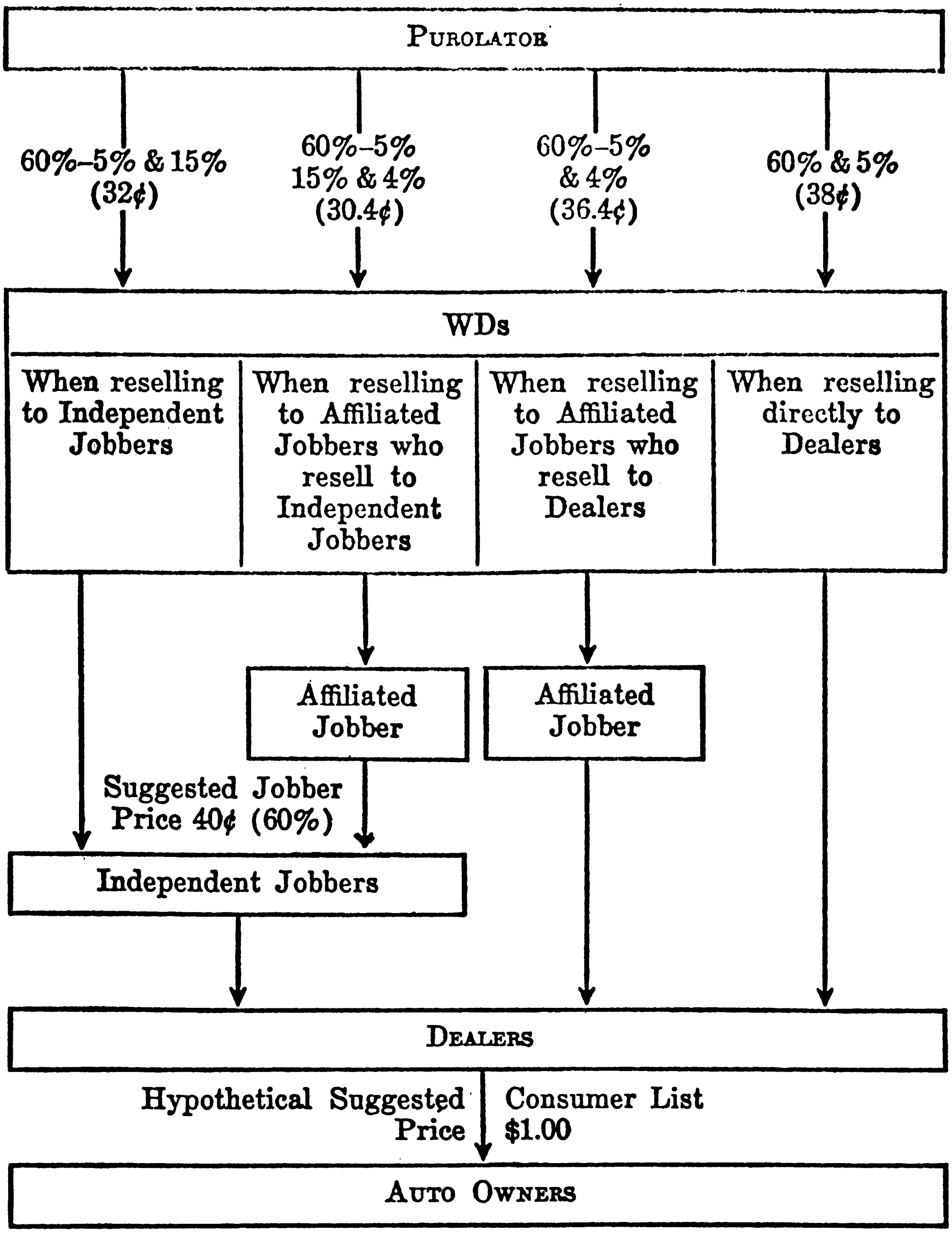
155/ Borman Food Stores, 81 F.T.C. 201, 208 (1972) (Elman, Comm., dissenting).

four cents on every head of lettuce sold in the country would be a significant amount," and that if these proceedings had any economic impact it would be an inflationary one, the majority members believed that the Commission had no discretion in the matter and was compelled to proceed with these complaints, even though their issuance might be antithetical to fundamental national policies declared by Congress and the President.

(ii) Inhibiting More Efficient Forms of Distribution

The Robinson-Patman Act creates great difficulties for suppliers who operate "dual distribution" systems by which sales of goods are made directly to retailers in some instances, and in others to middlemen, such as warehousers, who then resell to retailers. Integral to such system is the "functional discount," which is a discount granted to different types of middlemen, such as wholesalers, and is designed to compensate the middlemen for assuming various distribution functions. The Robinson-Patman Act permits such discounts as long as each businessman performing a particular function gets the same discount for the performance of such function, and so long as the discount reflects the purchasers' relative positions in the chain.

Cases involving functional discounts are often quite complex, sometimes involving one firm's sales to direct-ship retailers, wholesalers, and integrated wholesaler-retailers. The reprinted diagram from a court decision in one such case is illustrative (see next page). A difficulty with the Act's regulation of functional discounts is that, with respect to purchasers on the same functional level, a discount reflecting a manufacturer's cost saving will be upheld; discounts reflecting the value to the manufacturer of purchaser's


PUROLATOR
60%–5% & 15% (32¢)
60%–5% 15% & 4% (30.4¢)
60%–5% & 4% (36.4¢)
60% & 5% (38¢)
WDs
When reselling to Independent Jobbers
When reselling to Affiliated Jobbers who resell to Independent Jobbers
When reselling to Affiliated Jobbers who resell to Dealers
When reselling directly to Dealers
Affiliated Jobber
Affiliated Jobber
Suggested Jobber Price 40¢ (60%)
Independent Jobbers
DEALERS
Hypothetical Suggested Price
Consumer List $1.00
AUTO OWNERS

service will not. Thus, the Commission has struck down the granting of special discounts to "special function" distributors but not to competing regular distributors.156/ The effect is to prevent distribution systems from becoming more efficient or assuming new shapes:157/

> Such a test obviously discourages buyers from taking on additional distributive functions to those performed by their competitors, however beneficial that might be to the economy, since they cannot be rewarded for doing so. And where the extra cost of rendering the additional distributor function approximates the amount of the discount, there is no real basis for a finding of competitive injury.

Moreover, those enforcing the Act determine the functional level of a "dual function" purchaser by reference to the function he performs "furthest" from the manufacturer. Under this rule, an integrated wholesaler-retailer, for instance, is considered a retailer. Consequently, a discount granted to the integrated buyer must be justified by cost savings to the manufacturer, vis-a-vis its sales to other retailers. On the other hand, discounts to single-function wholesalers need not be cost justified and are lawful as long as they reflect an appropriate allowance to the wholesaler for performing the wholesaling function. Thus, the independent wholesaler is often entitled to a larger discount than the integrated purchaser.

A singularly perverse impact of this feature of the Act is its impairment of the ability of small retailers, particularly in the

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156/ Mueller Co. v. FTC, 323 F.2d 44 (7th Cir. 1963), cert. denied, 377 U.S. 923 (1964).

157/ Prepared Statement of Paul H. LaRue, Subcommittee Hearings, pt. 2 at 229.

automotive parts industry, to replace their reliance on independent middlemen by establishing cooperative wholesale operations. An example of this effect is found in the Alhambra Motor Parts case.158/ There a cooperative in its warehouse capacity bought large parts inventories on its own account, stored them at its own risk, and filled members'orders out of the cooperative's inventory. The Federal Trade Commission ruled that since the cooperative was owned by retailer members, any discounts to the warehousing cooperative would be considered as discount payments to the retailer members. The Commission, therefore, ruled that since the retailers were in competition with other retailers not members of the cooperative, any discount to the cooperative would have to be cost justified. After analysis, the Commission rejected the justification offered and struck down the discounts.

The Commission's ruling did not affect the size of discounts granted to the independent wholesaler-distributors, because these distributors were not in competition with any of the retailers. As a result, the decision guaranteed the continued existence of the independent wholesaler-distributors: without the ability to get the same discounts as the independent wholesalers, the cooperatives owned by small retailers were placed at a competitive disadvantage. It is not surprising, then, that the association representing the independent

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158/ Alhambra Motor Parts Inc., 68 F.T.C. 1034 (1965).

wholesaler-distributors submitted a statement to the Review Group in favor of preserving Robinson-Patman.159/

(iii) Inhibiting Backhauls

Inefficiency in distribution also results from the Act's restraints on "backhaul allowances" in the food and other industries. Many manufacturers sell their merchandise on a delivered price basis: manufacturers charge the same price to all purchasers in a given geographical region without regard to actual differences in transportation costs for each customer. Under this system, a selling price of a good includes the price of manufacture plus the average cost of transportation incurred in selling to all the supplier's customers. The use of delivered pricing permits a food manufacturer to remain price competitive in a particular region by removing any disadvantage in selling to retailers who are relatively more distant from the manufacturer's warehouse than from the warehouse of the manufacturer's competitors.

Many grocery chains and cooperative wholesalers operate large private truck fleets to serve their affiliated stores. After delivering goods to retail outlets, these trucks may return empty near the manufacturer's points of distribution. It would save both fuel and money for these trucks to pick up goods from the manufacturer's warehouse on the way back, thus eliminating the need for the manufacturer to hire a common carrier to deliver his goods to the warehouse of the chain or coop. Moreover, if a common carrier is hired, its

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159/ Statement of Basil Mezines, DCRG Hearings. His statement indicated that a benefit of such rulings was that, in order to remain in business, any cooperative of retailers had to be open to all retailers in an area. Statement at A-13.

truck may very well return empty to the city of origin. However, backhauls by food wholesalers will not be advantageous to them unless they can be recompensed for the extra expense involved. The Robinson-Patman Act prevents full compensation for the backhaul expense, and thus discourages backhaul and encourages the running of empty trucks.

The FTC has ruled 160/ that a manufacturer may utilize a delivered pricing system, but may only give a uniform allowance to those retailers who pick up their own merchandise. In other words, the FTC permits a manufacturer to give its customers only two alternatives: a uniform delivered price or a uniform FOB (Free on Board) price. The allowance of a uniform pick-up price as the only alternative to the otherwise prevailing delivered price results in inefficiencies in two ways. First, it encourages merchants who are very near the pick-up point to send trucks out for the specific purpose of taking delivery of their own merchandise and receiving the backhaul allowance when it would actually cost less for a common carrier to deliver the merchandise. Second, it discourages merchants who are distant from the manufacturer from diverting empty returning trucks to pick up merchandise. This happens when the uniform delivered allowance would not be sufficient to cover the extra cost of diverting that empty truck somewhat from the most direct route back to the merchant, in spite of the fact that a sufficient allowance would also cost the manufacturer less than the cost of common carriage.

160/ FTC Advisory Opinion 147 (1967) as clarified by Advisory Opinion 483 (1973). See 16 C.F.R. §§ 15.147, 15.483 (1975).

One witness who appeared before the Review Group, representing a cooperative food wholesaler located in Kansas City, Kansas, testified that one of the food manufacturers supplying his company grants a uniform backhaul allowance of 24 cents per hundred weight. This amount, which was calculated on advice of counsel, represents the cost of delivery in St. Louis, Mo., the city in which the manufacturer's distribution center is located. The witness reported that his trucks go to within 60 miles of St. Louis, but that they could not afford to go those extra 120 roundtrip miles at the 24-cents allowance rate. The amount necessary to make it profitable for the cooperative to pick up the goods, though greater than the 24-cent allowance, would nevertheless be less than the actual freight of 99 cents paid by the manufacturer for common carriage of the goods to the cooperative's warehouse. Because of the inability of the manufacturer to obtain FTC permission to grant a backhaul allowance based on the manufacturer's actual cost of freight (in spite of the wholesaler's desire to pick up his own goods), the wholesaler's truck must run empty and another vehicle must be dispatched to deliver the goods. 161/

Both Albert Rees, then head of the Council on Wage and Price Stability, and Frank Zarb, head of the Federal Energy Administration, have written to the Federal Trade Commission in favor of permitting cost justified backhaul allowance. The food industry advisory committee of both the National Commission on Productivity and the Federal

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161/ Testimony of Louis Fox, DCRG Hearings, Tr. 95-106, 115-117.

Energy Administration have developed estimates of the magnitude of cost savings which could be realized if backhaul was fully utilized in the food industry. Though subject to some qualification, these figures indicate a potential savings of up to 100 million gallons of fuel and cost savings in the neighborhood of 300 million dollars per year. 162/

While the full utilization of backhaul is constrained as well by factors other than Robinson-Patman (*e.g.*, the Interstate Commerce Act) the available evidence indicates that the threat of Robinson-Patman violations plays a not insignificant part in the decision of manufacturers to refrain from offering backhaul allowances and in the lessening of the potential savings from such programs.

c. The "Proportionality" Test For Allowances Leads to Needless Allowances and Much Confusion in Distribution

Sections 2(c) and (d) of the Robinson-Patman Act require that the furnishing of allowances, facilities, and other services to purchasers be made on proportionally equivalent terms to all purchasers. This is another *per se* rule, requiring no showing of competitive impact, and ameliorated only by the meeting competition defense.

The statute imposes extremely complex and burdensome requirements on schemes for promotional and other allowances. For example, how does a reasonable businessman calculate the proportional equivalent to a small drugstore of the manufacturer's employee who demonstrates a

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162/ Letter from Frank Zarb to Lewis Engman, Chairman, Federal Trade Commission, dated August 15, 1975; Letter from Albert Rees to Lewis Engman, dated April 1, 1975; Testimony of Louis Fox, *DCRG Hearings*, Tr. 93.

product on the premises of a large high volume department store?

Under the Fred Meyer decision 163/ the manufacturer is responsible for insuring that the allowances given to an independent wholesaler are passed on proportionally to retailers who purchase from that wholesaler. This interpretation of the Act has generated additional regulations: The Federal Trade Commission issues so-called "Fred Meyer Guides" published in the Code of Federal Regulations, 164/ which detail the conditions which must be obeyed in order to avoid an FTC enforcement action. Even attorneys favorable to Robinson-Patman have concluded that the allowances requirements set out in these guides are so complex as to be totally unworkable. 165/ Moreover, the guides compel firms to provide useless or unwanted service or to forego service which is both useful and desired: 166/

> Under the standard of proportionality, concerns have had either to buy undesired advertising and provide services they regarded as valueless, on the one hand, or refrain from providing service or purchasing advertising they regard as desirable on the other.

This is because allowance programs cannot be limited to situations where use of the allowance would result in a benefit to the seller

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163/ Fred Meyer, Inc. v. FTC, 390 U.S. 341 (1968).

164/ 16 C.F.R. § 15.240.

165/ Testimony of Jerrold C. Van Cise, Subcommittee Hearing pt. 2 at 217.

166/ EDWARDS, *supra* note 107, at 629.

equal to the expense of the program. Manufacturers must thus forego promotional programs which would benefit the manufacturer only if they could be limited to purchasers who could fully utilize them.

An example of the exercise required by the Act as applied under FTC rules was given by a former RCA vice-president. RCA has a program of cooperative advertising allowances under which dealers are granted allowances for advertising appliances under both the dealer's and RCA's name. In order to comply with Robinson-Patman, RCA instructed its wholesalers to offer the same per-appliance allowance to each retailer-customer and to require the retailer to provide written acknowledgment of the offer. In the case of many Mom and Pop stores the required offer was a meaningless gesture: the cooperative allowance, given the small sales volume on which it was based, would be insufficient to purchase anything but a small classified advertisement. Eventually, some small dealers requested termination of the practice of offering a useless allowance; these small stores preferred that the funds designated for their use go to <u>major accounts</u> which received sufficient cooperative allowances to take out large newspaper advertisements. With typical ingenuity, the small stores recognized that they could compete by posting the large ads (with lower prices) in their own window fronts. 167/

d. Robinson-Patman Handicaps Smaller Retailers By Restricting Supplier Ability to Respond to Pricing Challenges from the Smaller Businessman's Competitors

An ironic and unforeseen impact of Robinson-Patman is that it discourages suppliers from helping smaller customers meet their price

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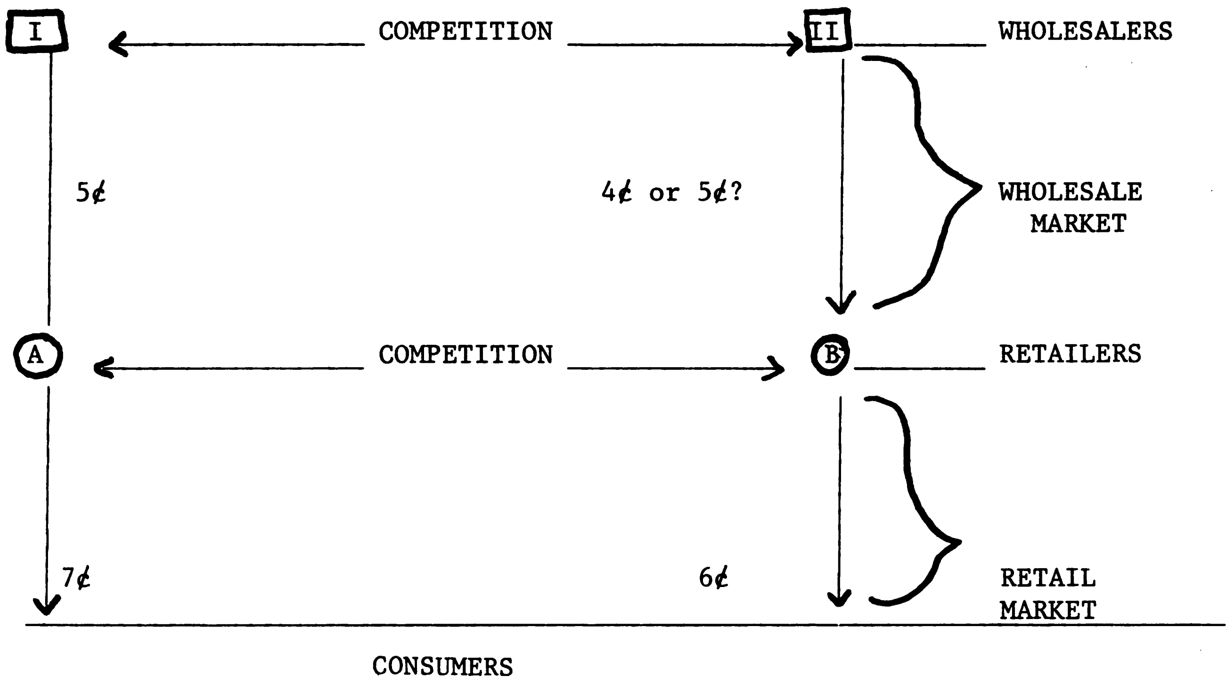
167/ Testimony of Martin Bennett, <u>DCRG Hearings</u>, Tr. 81a-82.

competition. The meeting competition defense, under the Act, does not permit a supplier to help one of his customers meet a lower price charged in the retail market by a competitor of that customer unless that lower price itself resulted from a lower price from the competitor's supplier.



How the rule works may be seen in the above diagram. Retailer A is losing business to Retailer B because Retailer B is charging consumers 1 cent less than A. Retailer A goes to Supplier I and asks for a 1 cent discount. Supplier I can provide the requested discount only if Supplier II is charging his customer less than Supplier I charges his. If II is charging 5 cents, the discount cannot be given; if II is charging 4 cents, the discount can be given.

This doctrine had its origin in Federal Trade Commission v. Sun Oil Co. 168/ In that case, a Sun Oil dealer was located directly across

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168/ 371 U.S. 505 (1963).

the street from the only franchise dealer in town of a competing brand of gasoline. When that station began to sharply cut its price, Sun Oil decided to assist its dealer meet the competition by granting the Sun dealer a special low price. The low price was continued for a period of two months, thereby enabling the Sun dealer to survive the price war with the station directly across the street.

The Supreme Court upheld a Federal Trade Commission finding that the discount given by Sun to its threatened dealer violated Robinson-Patman because it might adversely affect other Sun dealers in the region. The meeting competition defense was not satisfied because there was no proof that the lower prices charged by the gas station across the street from the Sun dealer were the result of the low cost of gasoline it purchased.

The Court's opinion suggested that such discount could be given, absent a successful meeting competition defense, only on the basis of a complex system of zone prices in the region designed to prevent any adverse effects among dealers of the Sun brand of gasoline. However, it is unlikely that a supplier would be willing to establish a complex system of zone prices or to reduce prices to all dealers in a region in order to help protect a single dealer. In such a case, the small businessman who is directly affected by competition from a competing brand might well be sacrificed to the requirements of Robinson-Patman.

A situation where Robinson-Patman thus can injure small dealers may arise when a competing manufacturer sells a special model at a low price to a single outlet in an area or "dumps" a slow moving model at a low price to a few outlets. Of course, such selective selling by the competing manufacturer is lawful since the Act does not require the manufacturer to make the low-cost model available to all its dealers in the area. Yet, other manufacturers and wholesalers who sell equivalent models to all retailers in a region may not be able to assist their dealers because of the above difficulties of the meeting competition defense.

A witness before the Review Group gave an example of such a situation. In the home appliance industry, small independent dealers may suddenly confront an especially low price being advertised for a competitive model of another brand. The witness stated that his company, RCA, believed that the Mom and Pop appliance dealers were an important part of the distribution system and therefore deserved help in such circumstances. But help often could not be provided, for it was frequently impossible to ascertain whether the large outlet was charging the low advertised price as a loss leader or as a result of a special allowance from its supplier. Without such information RCA's wholesalers would risk Robinson-Patman liability if they gave smaller dealers a special allowance in order to help them match the competing price. When asked whether he knew of any instances of an independent distributor wanting to help the small businessman meet competition but being prevented from doing so by Robinson-Patman he responded: 169/

> Yes. I know of a number of instances where there
> was a distinct interest in helping the smaller

169/ Testimony of Martin Bennett, DCRG Hearings, Tr. 84.

store. And after all matters had been searched, it appeared that price was the only way out of the problem. Yes, they would hold up on the basis of the Robinson-Patman Act.

e. Robinson-Patman Places an Undue Regulatory Burden on Small Businessmen

The above discussion shows that Robinson-Patman imposes many arcane, complex regulations on the conduct of business activity. Of course, when the Federal Government and its regulatory agencies impose such burdens on businessmen, the legal profession receives handsome financial rewards, and the businessman's ability to conduct his operations on the basis of his own best judgment is correspondingly diminished. As Jonathan C. Rose, Deputy Assistant Attorney General for the Antitrust Division put it: 170/

> Not only does the Act thus provide much business for corporate house counsel . . .but actually imposes a hardship on smaller businesses who do not have their own antitrust counsel, and so must increase their expenditures on legal advice. The end result is that all too often, the ultimate pricing strategy must be decided by attorneys and not those with expertise in marketing.

More importantly, as actually enforced by the Federal Trade Commission, the Robinson-Patman Act in ironic contradiction to the professed intentions of its sponsors has actually placed an unfair enforcement burden on smaller companies. The Federal Trade Commission's director of its Bureau of Economics frankly admitted: 171/

> I had not fully realized until I came to Washington how unfairly the burden of federal regulation and

170/ Speech of Jonathan C. Rose before the Legal Affairs Committee of the Grocery Manufacturers Ass'n, October 29, 1975, at 13.

171/ Prepared Statement of F. M. Scherer, Subcommittee Hearings, pt. 2 at 145.

> antitrust enforcement falls upon small as compared to large companies. The corporate giants can and do maintain stables of highly skilled attorneys to advise them how to stay clear of the law and defend them if they nevertheless run afoul. Smaller firms are less able to afford such counsel, and the law firms they retain typically lack the specialized knowledge needed to cope with the body of statutory, case and regulatory law as complex as Robinson-Patman. As a result, they are more likely to get into trouble and to settle by consent if a complaint is brought. . . . I had also understood little about the value system of government antitrust attorneys. What I have learned since joining the Commission staff is that many attorneys measure their own success in terms of the number of complaints brought and settlements won. In the absence of broader policy guidance, therefore, the typical attorney shies away from a complex, long, uncertain legal contest with well-represented giant corporations, and tries to build up a portfolio emphasizing small, easy-to-win cases. The net result of these . . . broad propensities is that it is the little guys, not the giants who dominate our manufacturing the trade industries, who typically get sued.
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> This fact emerges strikingly from an analysis of Robinson-Patman Act enforcement patterns recently conducted by the Bureau of Economics staff.

In the study mentioned by Mr. Scherer, an analysis was made of 114 complaints involving 569 respondents filed under the Robinson-Patman Act between 1961-1974. Section 2(c) brokerage complaints were excluded because of the inherently small size of the brokerage respondents.172/ The results of the analysis showed that of the 569 respondents, only 25 or 4.4 percent were large enough to be included in the Fortune 500 directory of businesses for the year in which the complaint was issued. An analysis of the standard industrial, credit, and marketing

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172/ It should be noted that of the 439 final FTC enforcement orders issued from 1936 to 1969, 180 of them concerned brokerage. See text at note 153 , *supra*.

guides reported the status of 216 respondents. Of those 216 listed respondents only 35 had sales exceeding $100 million while 101 definitely had sales of less than $10 million. The remaining 354 respondents could not be located in any directory, and were presumably of very small size.

3. Conclusion

The Robinson-Patman Act has several significant costs to society. Its most pernicious effects are its reinforcement of pricing rigidity among sellers in oligopolistic industries, the introduction of pricing inflexibility, and the encouragement of price discussions among competitors which may lead to violations of the Sherman Act. To the extent that new entry is impeded by Robinson-Patman, the Act also serves as an artificial "barrier to entry" protecting highly concentrated local markets. Finally, because of restrictions on purchaser behavior, the Act discourages buyers from engaging in "hard bargaining" with large sellers, further enhancing their ability to charge non-competitive prices.

This direct protection by Robinson-Patman of higher prices is compounded by the higher costs which are generated by the Act. The provisions of the Act tend to preserve a layer of additional middlemen even though integration of certain distribution functions might be more efficient. The Act encourages the granting of useless promotional allowances and the proliferation of product brands and physical differences in manufactured goods. Moreover, by reducing the ability of businesses to utilize empty truck backhauls for the carrying of merchandise, Robinson-Patman encourages the wasteful use of energy and other scarce resources.

Finally, Robinson-Patman can actually make it more difficult for manufacturers and distributors to help small businessmen meet competitive challenges. At the same time, the brunt of enforcement of the Act has fallen on smaller businesses, and increased legal and administrative costs associated with this regulatory scheme are relatively more burdensome for smaller enterprises.

The Report in the next two chapters will show that the adverse effects of Robinson-Patman were the inevitable result of the process by which Congress adopted this legislation; that Congress justified the statute on the basis of faulty economic assumptions and illusory objectives; and that Congressional misunderstanding of the competitive process guaranteed the enactment of a statute which would dramatically distort rather than preserve the beneifts of that process.

Chapter III. THE ECONOMIC, POLITICAL AND LEGISLATIVE HISTORY OF THE ROBINSON-PATMAN ACT

A. The Economic and Political Crisis of the 1930s.

Much of the economic thought of the 1930 s was preoccupied with recovery from the depression. No legislature convened during that period could ignore the catastrophic failure rate of businesses of all sizes, declining wages, and the rapid decrease of the gross national product. 173/ The disruption of economic life was such that ordinary people lost confidence in the free enterprise system; people clamored for government protection, not competition. The spirit of the times was captured in the testimony of one Review Group witness: 174/

> [T]he Depression understandably generated desperation and fear, a desire to do anything, something, anything. It was a period of profound disenchantment with competition, which was widely thought to have contributed to the deflation of the day. This disenchantment was fully reflected in what I would call the 'Blue Eagle Spirit' of protectionism and government supervised cartels.

This compulsion to regulate rather than allow competition was more than a popularly held sentiment; loss of faith in the free enterprise system was pervasive even in academic and intellectual circles. 175/

173/ J. GALBRAITH, THE GREAT CRASH (1954); W. CHANDLER, AMERICA'S GREATEST DEPRESSION (1970).

174/ Testimony of Donald I. Baker, DCRG Hearings, Tr. 268.

175/ Id., 276-77.

> That [the Blue Eagle Spirit] was alive in 1936 is nicely shown in a book written that year, appropriately entitled, The Decline of Competition. Its author was a young economics professor at Columbia University named Arthur Robert Burns . . . . He stressed on the first page 'a growing doubt concerning the capacity of competition to survive, or where it survives to produce satisfactory results.' Remember, this was in 1936, the year the Robinson-Patman Act was enacted. Then he went on to say, 'Adam Smith's unseen hand has been brushed aside by the half-seen hand of self-government in industry, and it cannot be restored by law. Contemporary developments all point in one direction, viz. that leaving it to competition is a state policy with which no one is satisfied and upon the meaning of which there is no general agreement.'

Almost simultaneously with the depression came a second, and to some equally threatening development, a revolution in distribution. 176/ During the late 1920's and early 1930's chain stores grew rapidly as a new channel of distribution. The Federal Trade Commission, in a final report summarizing an extensive six-year study of chain stores, found a "marked increase" in the number of chain stores reported in operation; 177/ it found that the number of operating chain stores increased from 58 in 1900 to 1718 chain stores in operation by 1928. 178/ Significantly, this chain store growth took place during the period of increased small business mortality. Congress perceived the chain store growth and small business mortality as related; it is not surprising, therefore, that the changes in patterns of distribution were viewed with alarm.

176/ The dynamics of the evolutionary cycle in distribution are described in Section B(1) of Chapter IV, pages 170-180, infra.

177/ FTC, FINAL REPORT OF CHAIN STORE INVESTIGATION, S. DOC. No. 4, 74th Cong., 1st Sess. (1935) (hereinafter cited as 1935 FTC CHAIN STORE REPORT).

178/ S. DOC. No. 100, 72nd Cong., 1st Sess. 54 (1932).

It is unclear, however, whether the small business sector was actually threatened more than any other segment of the economy. While the FTC study focused mainly on the growth of chains in terms of numbers, rather than market share by sales, its figures on sales showed that in 1929 chains, taken as a whole, accounted for less than 20 percent of all sales made in retail distribution. 179/ The House Judiciary Committee, in its hearings on the Robinson-Patman Act, nevertheless believed that the chains were much more powerful. Representative Wright Patman, testifying before the Committee, stated that only 18 percent of the cash business in groceries was done by independents. 180/ And during the debates on the floor of the House of Representatives figures from the Census of American Business were introduced to show that the chain stores' market share by sales ranged from 44 percent to 95 percent. 181/

The evidence concerning the mortality rate of small businesses was also far from clear, although it is undisputed that the failure rate for businesses of all sizes increased greatly between 1925 and 1932. 182/ Opponents of the Robinson-Patman Act offered testimony tending to show that between the years of 1929 and 1933 the number of small businesses had in fact increased and that the number of chain stores had decreased. 183/

179/ 1935 FTC CHAIN STORE REPORT 4.

180/ Hearings on H.R. 8442, H.R. 4995, H.R. 5062 Before The Committee on The Judiciary of The House of Representatives 5, 74th Cong., 1st Sess. (1935) (hereinafter cited as Sumners Hearings).

181/ 80 CONG. REC. 8116 (1936) (Remarks of Rep. Patman).

182/ DUN & BRADSTREET, THE BUSINESS FAILURE RECORD, 1974 cover p. 2 (1975).

183/ Sumners Hearings 132.

The members of the Committee, however, preferred to rely upon their own impressions and anecdotes from constituents. With respect to the proffered statistics concerning business failure rates, Chairman Sumners said, "[t]he average man would be very much astonished, because we have been walking around in our little villages seeing where the independent store used to be there is now a chain store." 184/

Proponents of the legislation argued that the small independent retailer was in great danger of disappearing from distribution altogether: 185/

> The result is, I believe it is the opinion of everyone who has studied this subject, that the day of the independent merchant is gone unless something is done and done quickly. He cannot possibly survive under that system. So we have reached the crossroads; we must either turn the food and grocery business of this country - now, that is just one division - we must either turn the food and grocery business of this country over to a few corporate chains, or we have got to pass laws that will give the people, who built this country in time of peace and who saved it in time of war, an opportunity to exist - not to give them any special rights, special privileges, or special benefits, but just to deny their competitors the special benefits that they are getting, that they should not be permitted to have.

Many legislators, then, sincerely believed that the small wholesaler and retailer were in immediate danger of extinction; they further believed that the chain stores, in pursuit of total monopolization, had caused the small businessman's plight.

Anti-chain sentiment became virulent. Emotions were so strong that many Congressmen would have supported a bill legislating the absolute prohibition of chain stores. For example: 186/

184/ *Id*.

185/ *Id*. at 5-6.

186/ 80 CONG. REC. 8136 (1936) (Remarks of Rep. Moritz).

> I do not know what our family would have done when I was a child if we had not used the book of the independent stores. We used the book of the friendly neighborhood grocery store. We waited until dad got paid and then paid the bill. You can not do that at the chain store. If that is radical, make the most of it. I believe the chain store should not only be curbed, but they should be eliminated, because the great harm they do far outweighs the little good they do.

The growth of the chain stores was furthermore seen as a personification of the many horrors of the depression. 187/

> I know, and the people of the country know, that the great majority of fair manufacturers and retailers and all those who favor a fair and square deal are in favor of this legislation. They realize that it will restrict the chain-store and mail-order octopuses which are gradually but surely destroying the small businessman in every section of the country.
>
> . . .
>
> The chain-store octopuses, mainly controlled by Wall Street financiers, must be restricted from unfair and discriminatory practices. Since the ethics of fair dealing seem to be unknown to them, these overlords must be prevented by legislation from obtaining special inducements, at the expense of independent dealers, through threats and coercion.

Anti-chain, pro-small business sentiment manifested itself in ways other than the Robinson-Patman Act. For example, just prior to the introduction of the Robinson-Patman Bill, Representative Patman had chaired a committee to investigate the lobbying practices of the American Retail Federation, an organization founded for the alleged purpose of lobbying in favor of the chain stores. The resolution authorizing this investigation gives some sense of the passion of the times. 188 /

187/ *Id*. at 8102 (Remarks of Rep. Sabath).

188/ *Id*. at 8105.

> Whereas it is apparent that said American Retail Federation is organized for the purpose of increasing the profits of big business, through lobbying tactics, designed to prevent small businesses from securing competitive opportunities equal to those enjoyed by corporations representing vast aggregations of capital; and
>
> Whereas it is apparent that the achievement of any or all of the purposes of said American Retail Federation will react to the detriment of the farmer, the wage earner, and the consumer, on the one hand, and will serve to injure the employers of labor and the laboring man on the other hand; . . .

The anti-chain sentiment and the willingness to believe that the growth of chain stores (as part of an overall revolution in distribution) meant the total demise of the independent retailer were not isolated phenomena; they were part of the national mood which desired the protection, during a particularly difficult period, of a disappearing way of small town life threatened by the perceived encroachment of big business, the big city, and Wall Street. It is evident that a number of legislators saw the changing way of life in the small towns of the country as a national emergency requiring a legislative remedy. Nostalgia for the small town way of life is found in a number of different expressions of support for the Robinson-Patman Act. One Congressman expressed sentiment for the small grocery store as a social center: 189/

> You know there is a certain sentiment and romance about the corner or crossroads grocery store. There formerly, and there now, exists the skit and whittle club. You

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189/ Id. at 8135 (Remarks of Rep. Nichols).

> know, where the boys gather around the stove in the winter, sit around its red-hot fire, chew tobacco, spit on the bowl, and listen to it sizzle, and settle the problems of the Nation, and the problems of the community.

The passing of the independent retailer, it was feared, would eliminate an element of charity from life: 190/

> No chain store in my community has ever carried the widow Jones and her two little kids on their books for 30 days or 60 days or any length of time while she was getting together a few pennies to pay for the things which she had to buy from the store.

And another Congressman attacked the chain stores for selling on Sunday: 191/

> I am not a Sabbatarian, but I do believe in a proper observation of that day from the standpoint of religion, rest, and pleasure.
>
> In almost every city in this country today you will find a group of chain stores, under the guise of drug stores, selling every article under the sun and keeping open 18 hours on Sunday as well as the day before, the Sabbath of Moses.

In the midst of the concern about a disappearing way of life, it would have been surprising if Congress had not expressed determination to save the independent merchant and the type of community he served: "As lawmakers, can we do something that will sort of preserve the communal life in those little centers?" 192/

Robinson-Patman Act supporters, lapsing at times into a conspiracy theory of chain store development, saw big business, Wall Street, and the big city allied against this cherished way of life. 193/

190/ Id.

191/ Id. at 8128 (Remarks of Rep. Shannon).

192/ Id. at 8133 (Remarks of Rep. Dirksen).

193/ 79 CONG. REC. 11575 (1935) (Remarks of Rep. Patman).

> I am convinced that there is a conspiracy existing between a few Wall Street bankers and some of the heads of the biggest business institutions in this Nation to absolutely get control of retail distribution. They expect to do that through the chain-store system.

At times, the debate took on decidely anti-New York City overtones: 194/

> This is a bill to protect the farmers of this country, I say to my distinguished friends from the heart of New York where holders of privilege reside. I heard one witness before the Rules Committee say that 90 percent of the people affected by this bill live in two congressional districts in New York City. I do not take issue with that statement. I believe it is absolutely true, that 90 percent of them live in those two congressional districts.

Thus, the mood of Congressmen of the 1930's reflected the crisis temper of the times. Indeed, as elected representatives with special responsibilities to help right matters, Congressmen were laboring under the kind of pressure likely to distort perceptions and to produce ill-conceived solutions.

B. Legislative Responses to the Crisis

The Robinson-Patman Act was not the sole legislative response to the depression and the chain stores; it was but one of a series of attempts to preserve the existence of the independent retailer and the way of life he represented.

The National Recovery Administration, 195/ in an ambitious attempt to relieve the nation's economic ills, sought to impose stringent regulation on the distribution process. The codes, in effect from 1933 to 1935, governed the wholesale function, for example, by protecting wholesalers from any attempted diversion of goods from that portion of the distribution chain.

194/ 80 CONG. REC. 8112 (1936) (Remarks of Rep. Patman).

195/ Ch. 90, 48 Stat. 195.

The wholesale code in many trades required that manufacturers recognize a minimum wholesale discount; if any manufacturer attempted to bypass a wholesaler by quoting a wholesale price to any other customer, the code mandated that all code members boycott the manufacturer. 196/

In the retail trade, the codes of fair competition attempted to set a floor under prices. This was accomplished in several ways, but the goal was always the same: to protect retailers from what was regarded as unfair price competition. Sometimes the codes prescribed the actual retail price; in other cases a formula was provided which set prices along a cost plus formula. In the retail drug code, code members were able to develop one of the most restrictive price control measures. The price below which no retail druggist could sell was defined as the manufacturer's wholesale list price in dozen lots. This effectively prevented any large retailer from obtaining or passing on discounts beyond those achievable by purchase in dozen lots. 197/

A significant goal of the NRA codes was the preservation of the channels of distributions which existed prior to the depression and which were threatened both by that phenomenon and by competitive changes in patterns of distribution. A report on the National Recovery Administration transmitted by the President to the House of Representatives 198/ explained conditions which motivated the NRA's experiment in distribution control: 199/

196/ B. ZORN & G. FELDMAN, BUSINESS UNDER THE NEW PRICE LAWS, 32-33 (1937).

197/ Id., 33-34.

198/ COMMITTEE ON INDUSTRIAL ANALYSIS, A REPORT ON THE OPERATION OF THE NATIONAL RECOVERY ADMINISTRATION, H.R. DOC. No. 158, 75th Cong., 1st Sess. (1937).

199/ Id. at 152.

> Changes in distributive methods throughout industry had brought old procedures for distributing goods into competition with new, and had upset price structures adapted to the older methods. Under the codes some regulations bound one concern but not its rival, while others bore severely upon a group to whose processes of doing business they were little adapted.
>
> The distributive controls of the codes were addressed to these disparities of practice, sometimes in an effort to equalize the impact of other code provisions, sometimes to offset advantages enjoyed by one form of distribution, and sometimes to establish the supremacy of the distributive practices of those who controlled the code authority.
>
> The most conspicuous changes in distributive methods were the performance of wholesale functions by manufacturers selling direct to retailers, and of retail functions by manufacturers selling through their own retail outlets; the rise of mail order houses, department stores, chain stores, and voluntary chains which performed wholesaling and even manufacturing functions; and the development of limited function wholesalers alongside those performing the full traditional function.
>
> In this reshuffling of distributive functions manufacturers and wholesalers came to compete with one another for the retailer's trade, and in some instances manufacturers, wholesalers, and retailers alike vied to do business with the large consumer. Each found cause for grievance in the rivalry.

Those aggrieved by the changes in distribution recognized that the traditional way of business could not simply be frozen in place; they focused, instead, on denying the mass merchandiser the cost advantages achieved through direct buying: 200/

> Most wholesalers recognized that they could not directly prevent manufacturers' sales to retailers. They accepted such sales as legitimate if the manufacturer had abandoned

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200/ Id. at 153.

wholesale channels of distribution entirely, or if he sold to retailers at prices comparable to those charged by the wholesaler. Their major point of resentment was the grant of low prices in direct sales by manufacturers.

The NRA report concluded, however, that the codes were of limited utility in controlling the channels of distribution. The program to control distribution was successful primarily where no organized opposition could be mobilized. Where there was disagreement between conflicting groups, the codes would be effective only with the active support of the NRA and its enforcement powers. But the Administration was reluctant to lend its support to direct attempts at preventing changes in distribution patterns. The NRA, therefore, did not achieve the rigid regulation of distribution that wholesalers and retailers desired. 201/

Entirely consistent with the goals of the ill-fated National Recovery Administration and the Robinson-Patman Act was a second device fashioned in the attempt to regulate the process of distribution, the Fair Trade Laws. The campaign for fair trade, orchestrated mainly by the National Association of Retail Druggists (NARD), "the nation's most powerful trade association," 202/ took place on two fronts: statutes on the state level authorizing resale price maintenance were enacted in 44 states between 1933 and 1940; and the Miller-Tydings Amendment 203/ to the Sherman Act, providing an antitrust

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201/ The NRA was declared unconstitutional in 1935. A.L.A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935).

202/ BUSINESS WEEK, August 28, 1937, p. 42, quoted in J. PALAMOUNTAIN, THE POLITICS OF DISTRIBUTION, 235 (1955).

203/ Ch. 690, Tit. 8, 50 Stat. 693.

exemption for state authorized resale price maintenance, was passed in 1937. The fair trade statutes allowed agreements between suppliers and distributors which, under certain circumstances, prescribed minimum prices for the resale of trade-marked or branded commodities. The use of fair trade allowed a manufacturer to set all margins at which his product was distributed and to eliminate price competition at the retail level.

The boldest legislative assault on the chain store development was mounted in the form of proposed chain store taxes. During the 1930's, many states passed a variety of chain store taxation measures, with rates ranging in severity from mildly annoying to frankly confiscatory. At the federal level, the chain store taxation movement continued when Representative Patman introduced a bill to levy a national tax on chains. The proposed tax would have been progressive, with the taxation on each outlet increased by the number of stores in the chain. Its most restrictive effect, however, was to attach prohibitive taxes to the extension of a chain into more than one state. Under the proposed bill, a chain would have been required to multiply the tax payable by the total number of states in which it operated. 204/ This formula would have resulted in imposing upon A&P, for example, a tax of $523 million on an annual net income of $9 million. 205/ The Patman Bill was defeated when the chain stores successfully forged an alliance with farm and labor interests. The farmers' support was due mainly to the food chains' actions in purchasing excess agricultural commodities which had

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204/ PALAMOUNTAIN, supra n. 202 at 176.

205/ F. ROWE, PRICE DISCRIMINATION UNDER THE ROBINSON-PATMAN ACT, 8 (1962).

threatened to drive farm prices down in 1936. Organized labor abandoned its anti-chain store stance when, in 1938 and 1939, A&P signed a series of favorable collective bargaining agreements with the American Federation of Labor. 206/

Far from being discrete legislative programs, the NRA, the fair-trade laws, chain store taxation and Robinson-Patman formed a continuum of Congressional response to the rapid and apparently threatening changes taking place in the familiar structure of the American marketplace. The approaches varied, but in each case Congress sought to deny to those pioneering new channels of distribution the advantages of economic technology which, Congress feared, would leave traditional forms of distribution far behind. Robinson-Patman remains as a legislative vestige of those times.

206/ PALAMOUNTAIN, *supra* n. 202 at 180.

C. Congressional Debate on Robinson-Patman

1. The Legislative Process

The original Robinson-Patman bill was introduced on June 11, 1935, two weeks after the demise of the NRA. The bill, as drafted by H.B. Teegarden, counsel for the United States Wholesale Grocers Association, 207/ sought to attain an important goal embodied in the NRA codes, the protection of the three-tier distribution system. The original bill's proviso to its prohibition on price discrimination reveals that purpose: 208/

> [T]hat nothing herein contained shall prevent differentials in prices as between purchasers depending solely upon whether they purchase for resale to wholesalers, to retailers, or to consumers . . . nor differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods [or] quantities in which such commodities are to such purchasers sold or delivered.

This language contemplated a pricing system under which discounts would be available solely on the basis of a buyer's function in the chain of distribution, that function being defined by reference to the class of customers to whom the purchaser sold goods. Thus, a customer who purchased goods for resale to consumers would, by definition, be classed a retailer and denied a wholesaler's discount. And while the original bill appeared to provide for discounts on account of cost savings, the drafter of the bill contemplated a restrictive interpretation which would require that

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207/ Sumners Hearings 9.

208/ Id., at 1.

all of a manufacturer's overhead cost be spread equally over all units produced, thus limiting the amount of the price reduction that could be granted to a purchaser whose order did not utilize all overhead facilities. 209/ The original bill, therefore, would have established a rigidly defined system of functional discounts but discouraged quantity or other discounts tending to shortcut the traditional chain of distribution.

After the introduction of the Robinson-Patman Bill, and only a few days after the introduction of a similar companion bill in the Senate, the House Committee on the Judiciary chaired by Representative Sumners began its hearings on July 10, 1935. These hearings were to last but five days. Two bills sponsored by the Federal Trade Commission, implementing the conclusions and recommendations of its six year chain store study, introduced by Representative Mapes, were also assigned to the Sumners' committee. In spite of the FTC's extensive record on the chain store phenomenon, the two Commission-sponsored bills were never considered.

209/ Sumners Hearings 34. The reasoning is demonstrated by attorney Teegarden's explanation of cost justification:

> The bill does not permit [a] chain to demand price discounts representing a proportional share of the manufacturer's overhead which it fails to utilize.
>
> For illustration: Suppose manufacturer A maintains a system of branch sales offices and a corps of traveling salesmen for the purpose of canvassing and selling to the wholesale trade, and that the costs of this sales organization, including its overhead, represents 25 percent of his gross sales. Suppose then that chain X comes to A's headquarters office and offers him a large order for delivery direct to his chain retail outlets throughout the coming year and demands on that order a 25-percent discount on the plea that it has not required

(footnote continued)

The Sumners committee hearings consisted of a debate between wholesaler and small retailer organizations on the one hand,210/ and

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(footnote continued)

> the services of A's selling organization in any respect. If the same additional quantity of business had been sold to A's wholesaler customers it would have cost him, say, 3 percent more for salesmen's traveling expenses and perhaps salaries of some additional salesmen, but otherwise would have been absorbed under his existing sales overhead.
>
> In such case the chain might be given the 3-percent discount but not a 25 percent discount. The manufacturer is not able to abandon his whole selling organization merely by reason of the order of this chain, nor is he able to reduce his costs to an amount representing 25 percent of this chain's order. He does save 3 percent, however, as compared with the same amount of business sold to his other customers, and that 3 percent therefore represents the difference in cost of sale "resulting from the differing methods * * * in which such commodities are as to such purchasers (namely, the chains and the independents) sold or delivered." If the manufacturer would feel safe in abandoning his independent customers entirely and selling only to chains who called at his headquarters in this fashion, so that he might abandon entirely his sales organization and save the 25-percent overhead which it represented, then he might possibly sell to such chain at 25 percent less than his competitor who continued to serve the independent trade. But every practical manufacturer knows that if he should commit himself to such a change in his sales policy, he would soon cease to be an independent manufacturer and would become merely the manufacturing department of some chain organization. And every chain knows that when it buys in that fashion it has to bear certain costs of investigation of market conditions and movements that are otherwise sustained by the manufacturer through his sales organization.

210/ The problem facing those involved in traditional forms of distribution compelled a natural alliance between small retailers and wholesalers; the wholesaler's fate depended upon the continued survival of his customer, the small retailer. Small retailers, in turn, unable due to their size to engage in
(footnote continued)

large retailers and voluntary chains on the other. Of those witnesses appearing in favor of the legislation, five represented brokers, wholesalers or other middlemen, 211/ and two represented retailer organizations. 212/ The bill was opposed by two large retailers 213/ and one witness representing a voluntary buying group. 214/

The companion Senate bill, which had lain idle since its June 26, 1935, introduction, was suddenly reported out on February 3, 1936, by the Judiciary Committee without the benefit of its own hearings. 215/

> In its consideration of this bill, the committee has had the benefit not only of the diligent studies of its own members, but of the record of hearings on a similar bill (H.R. 8442) before the Committee on Judiciary of the House of Representatives, also of the hearings before a Special Committee on the House on Investigation of the American Retail Federation, and of the report of the Federal Trade Commission on its chain-store investigation (S. Doc. No. 4, 74th Cong., 1st Sess.). These have developed so fully the facts, trade and industrial, pertinent to the objects of

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(footnote continued)

mass, direct buying, were totally dependent upon their traditional supplier, the wholesaler. Thus the small retailer was often willing to follow the lead of the wholesalers in attempting to protect their mutual interest.

211/ H. B. Teegarden and J. H. McLaurin, United States Wholesale Grocers Association; Paul Fishback, National Food Brokers Association; Horace H. Herr, National League of Wholesale Fresh Fruit and Vegetable Distributors; Edgar Watkins, National American Wholesale Grocers Association.

212/ Roland Jones, Jr., National Association of Retail Druggists; John M. Pohlhaus, National Association of Retail Grocers.

213/ Robert E. Wood, Sears, Roebuck & Co.; Charles F. Adams, First National Stores, Inc.

214/ Gerard M. Ungaro, National Voluntary Groups Institute.

215/ S. REP. No. 1502, 74th Cong., 2d Sess. 2 (1936).

> the bill, together with representations of all interested parties for or against its specific provisions, that this committee has felt able to reach its decision without the delays of further hearings.

On the same day, a House Subcommittee chaired by Representative Utterback began the second set of hearings on the House bill. 216/ These hearings were to last but four days. By this time, favorable Robinson-Patman sentiment had crystalized; subcommittee members apparently thought of the further hearings as a forum for drafting a proposal rather than a debate on the merits. 217/

> Mr. Michener: This is just a continuation of the hearings that were held; is that correct?
>
> Chairman Sumners: I suppose it is, Mr. Michener.
>
> Mr. Michener: If that is true, we do not want--we might as well be frank about it now, but we do not want people coming in here with long speeches reviewing the whole thing.
>
> Chairman Sumners: That is right.
>
> Mr. Michener: If they have anything in addition to the hearings, that is what we would like. The case has been diagnosed, and it is the prescription that we want.

In spite of the Utterback Committee's inclination to consider the substantive debate closed, the second set of hearings produced substantial testimony

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216/ Hearings on H.R. 4995, H.R. 8442, and H.R. 10486 Before a Subcommittee of the Committee on the Judiciary of the House of Representatives, 74th Cong., 2d Sess. (1936) (hereinafter cited as Utterback Hearings).

217/ Utterback Hearings, 272-73.

opposing the Robinson-Patman Bill. In addition to repeat appearances by witnesses who testified before the committee chaired by Representative Sumners, the Utterback committee heard three manufacturers 218/ and two retailers 219/ oppose the legislation. The only new testimony favoring the bill was given by one wholesaler 220/ and one manufacturer. 221/

Apparently under pressure from manufacturers, agricultural producers, and mass retailers, who had been taken by surprise by the rapid legislative progress of Robinson-Patman, the Senate Judiciary Committee, on March 4, 1936, began a set of hearings on the Borah-VanNuys Bill. This bill was on its surface more stringent than the Robinson-Patman Bill, in that it provided for criminal penalties for certain price discrimination, but in reality was more liberal since it specifically allowed for quantity discounts. The hearings on this bill became a forum for airing the recently aroused sentiment against the Robinson-Patman Act; not one witness in the Senate Hearings supported the Robinson-Patman Act. While the Judiciary Committee filed no report on the Borah-VanNuys bill (the bill therefore died in committee), the hearings did weaken Senate support for the Robinson-Patman Bill.

218/ M. E. Kingman, representing various small rubber companies; W. B. Turner, Walker-Turner Co.; Norman Wiss, I. Wiss & Sons, Co.

219/ O. M. Kile, Mail Order Association of America; I. C. Fox, National Retail Dry Goods Association.

220/ Eugene C. Brokmeyer, Federal Wholesale Druggists Association.

221/ Paul S. Willis, Associated Grocery Manufacturers of America.

During the debate in the Senate, a number of amendments were offered to ameliorate the effects of the Robinson-Patman Act. At the conclusion of the debate, however, the Senate passed the Robinson-Patman Bill, amended by provisions similar to those of the Borah-VanNuys Bill. The intent was to pass to the conference committee the task of deciding between the two versions. 222/ The House, on May 7, 1936, passed the Robinson-Patman Bill with no mention of the criminal version added in the Senate.

The conference committee, apparently in deadlock, was unable to choose between the Senate and House versions. The ultimate result was passage of both Acts, with the Robinson-Patman House version becoming present Section 2, and the Senate version, with its criminal provisions, becoming present Section 3.

Congressional debate preceding the passage of the Robinson-Patman Act exposes the protectionist goals of the statute, and echoes the protectionist spirit of the times in general. 223/

> One of the duties of government is to protect the weak against the strong. I think this legislation will have a tendency to do that and, therefore, I am in favor of it.

It is clear, then, that while the supporters of Robinson-Patman spoke of enhancing competition, what they had in mind was protection of specific firms. 224/

222/ 80 CONG. REC. 6277 (1936) (Remarks of Senator Robinson).

223/ 80 CONG. REC. 8103 (1936) (Remarks of Representative Mapes).

224/ 80 CONG. REC. 9147 (1936) (Remarks of Representative Utterback).

> The difference may be illustrated where a nonresident concern opens a new branch beside a local concern, and with the use of discriminatory prices destroys and replaces the local concern as the competitor in the local field. Competition in the local field generally has not been lessened, since one competitor has been replaced by another; but competition with the grantor of the discrimination has been destroyed. The present bill is, therefore, less rigorous in its provisions as to the effect required to be shown in order to bring a given discrimination within its prohibitions.

While the Robinson-Patman proponents stressed protection of the small independent retailer as their primary goal, it is evident that a second group was also to be protected. Like the NRA, the necessary effect of the Robinson-Patman Act would be to preserve the traditional 3-tier distribution system (wholesalers, brokers, and other middlemen), from the marketing revolution. 225/ Many wholesaling groups therefore rushed to the support of the Robinson-Patman Act. It is interesting to note that in both sets of hearings held before the House committee, a total of only two retailers appeared in support of the Robinson-Patman Act, yet six witnesses representing middlemen supported the bill. Of those witnesses opposing the passage of the Act, four industry witnesses represented retailers, and no wholesalers appeared in opposition to the Act. 226/

225/ Thus, the Robinson-Patman Bill as originally introduced would allow differentials in price "depending solely upon whether they purchase for resale to wholesalers, to retailers, or to consumers . . ." This version of the Act, like the NRA codes before it, would have protected the middleman's position by codifying his right to a functional discount while denying that discount to direct purchasing mass retailers.

226/ Notes 211-22 and accompanying text.

The wholesalers' interest in the Robinson-Patman Act is clear in the legislative history; the mass merchandising revolution threatened to eliminate their function in the chain of distribution. An exchange between Chairman Sumners and Horace H. Herr, Secretary for the National League of Wholesale Fresh Fruit and Vegetable Distributors, indicates that the wholesaler proponents of the Robinson-Patman Act were as much interested in protecting their role in the process of distribution as in attacking the chains. 227/

> The Chairman: How are you adversely affected by the present practices and by the chain stores?
>
> Mr. Herr: By the present practices, not the chain stores alone, Mr. Chairman. We will take a large buying organization, any wholesale organization, or retail organization. The practice is that they step into our field and set up a brokerage company. That brokerage company goes to the producers and shippers buying for a parent concern that in many instances are retail outlets. They are rendering a buying service for the retail outlets; yet they assess the brokerage charge against the producer and the shipper.

Further along in his testimony, Mr. Herr makes it clear that his group objected to simplifying the process of distribution even though it would result in reduced prices to consumers. 228/

> [B]ut the effect is that you have reduced the price level on the whole crop of strawberries, and you have taken it right out of the pocket of the producer and the shipper. A gentleman of the committee asked yesterday whether or not the consumer got the

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227/ Sumners Hearings 70.

228/ Id., at 74.

> benefit. Yes; the consumer gets the benefit, but it is generosity with the producer and the shipper's money. You are taking it right out of his pocket and giving it to the consumer.

Against the threat to their function which many middleman perceived, the Robinson-Patman Act seemed an incomplete solution. One witness representing wholesale interests would have preferred an absolute prohibition upon direct buying by retailers, but acknowledged the unconstitutionality of his preference.229/

> Go just as far as you can to protect the public, but do not go far enough to make it unconstitutional. We are in favor of it; in fact, we would be glad to have, if we could, more legislation that would prohibit any manufacturer from selling to any retailer, or from selling to anybody but a wholesaler, but we do not believe you could do that, and we doubt if it would be in the interest of the public.

The middlemen witnesses opposed any changed in distribution which would tend to reduce the importance of their function. While the retail chains were the most visible threat, the development of retailer cooperatives or voluntary chains also was feared. Confirmation of the threat was provided in the testimony of a witness representing a cooperative food distributor: 230/

> Mr. Healey: Has the function that your organization performed tended to eliminate the jobber from this problem?
>
> Mr.Lazo: Yes, sir. It has to the extent that we have reduced the wholesale operations from an average between seven and eleven to an average

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229/ Utterback Hearings 289.

230/ Id., at 318.

> of between three and six, that is the wholesale operations. To that extent it, of course, tends to eliminate what used to be called the old-line jobber. That is quite obvious because of these retailers buying collectively through their own-owned organizations.

A careful reading of the legislative history shows that Congress intended to write a statute which would protect two groups--the wholesaler and the small retailer with whom he dealt. The apparent faith in the Act's ability to achieve those goals depended upon a few key assumptions about the way the marketplace worked.

2. The Nature of Congressional Economic Analysis

A central economic assumption upon which Congress proceeded was that the lower prices charged by the chain stores were due entirely to the discounts available to those stores. The committee's acceptance of this proposition was unquestioning: 231/

> The Chairman: Is the fact that the independent druggist is disappearing from the field due to increased cost of doing business by him, or due to differences between what his drug supplies cost him and what the cost to the chain is?
>
> Mr. Jones: There is no question that the latter part of your statement is true.

A second assumption made by Congress was that the growth of chain stores depended upon discriminatory pricing which created losses that had to be passed on to persons and firms least able to bear them. The supplier forced to give a discount to a chain store would recoup his loss by raising prices

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231/ Sumners Hearings 51.

to smaller independent wholesalers and retailers. The chain store, in turn, would recoup losses incurred in its below cost retail sales by raising prices to consumers in markets where competition already had been eliminated.

The proponents of the Robinson-Patman Act were inclined to view any differential in price charged to different customers as evidence of below cost selling. 232/

> Discriminations not in accord with sound economy generally involve an element of loss, either of the necessary minimum of profits or perhaps of actual costs, and this loss of profits must be recouped from the business of customers which do not receive the benfits of such discriminations.

Moreover, it was accepted that the losses resulting from such differentials would have to be made up by raising prices to other customers. 233/

> Mr. Michener: Do you mean to indicate the manufacturer selling to the retailer at a loss and then making it up somewhere else?
>
> Mr. Patman: In some cases; I have no doubt about it.

Similarly, where the chains were thought to set retail prices below cost, it was believed that the losses would be recouped in geographic markets where the chain store had achieved a monopoly. 234/

> This corporate chain desires to destroy the competitors around [its] thousand new stores. Under the existing

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232/ 80 CONG. REC. 3113 (1936) (Remarks of Senator Logan). The concept of "below costs" sales was not a clear one in the 1930's. For a discussion of current thought on the matter, see Sections A(2), (6) of Chapter IV.

233/ Sumners Hearings 12.

234/ 80 CONG. REC. 8116 (1936) (Remarks of Representative Patman).

system all they have to do is let these thousand stores have all their secret rebates obtained by reason of their purchases for all their 11,000 stores and this will enable the thousand new stores to soon destroy their competitors. When these competitors are destroyed, a thousand more stores can be opened and their competitors destroyed in a similar manner. The losses in one place are made up not only by the secret rebates obtained on total purchases but also on higher prices charged to consumers in areas where they already have a monopoly of business where their competitors have already folded up.

As a result of these assumed practices some legislators also believed that the long run result would be monopoly and unacceptably high prices.235/

Mr. Patman: But looking at this from the narrow point of view, what I consider--of course, other people differ with me, and they are just as honest in their views as I am--but I will say from the short-range point of view that possibly the consumer, if the chains were to get control of the grocery business of the country, that for a very short time they would get better prices--maybe they would. But we would have a monopoly and along with that monopoly would come higher prices and oppression, which will really result in either oppression of both producers and consumers or Government ownership.

Congress had before it, however, evidence that cast doubt on the validity of the economic assumptions and observations underlying the Robinson-Patman Act. Witnesses before the House Committees and the FTC's chain store investigation both questioned whether protection for the wholesaler and small retailer could be achieved by Robinson-Patman-type legislation. For

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235/ Sumners Hearings 6.

example, a number of witnesses before the Sumners and Utterback committees gave testimony to the effect that efficiency is a larger factor in lower consumer prices than the cost of goods sold. 236/

> Warehousing, order assembling, shipping, transportation and trucking, office accounting, particularly cost accounting, and innumerable other branches of the distribution field are the real factors in enabling a well-organized organization -- and that holds good with a corporate chain or a voluntary group or a retailerowned wholesaler group or a large wholesaler or large retailer -- to sell a quality merchandise on a lower cost to the consumer, more so than the mere factor of being able to buy certain commodities in the grocery line at a percentage lower than somebody else.
>
> I refer to the advantage that this economical distribution has for the benefit for the consumer and the producer, and when I speak of the producer, primarily he is the farmer. When we speak of the consumer, we speak of the modest wage earner, because in the last analysis he is the consumer of a vast volume of foods and merchandise that is consumed, and he is entitled to have the necessities of life distributed to him at the lowest possible cost of distribution.

A witness representing First National Stores of Boston attempted to demonstrate that cost is but the floor in pricing and that supply and demand will determine the ultimate price. 237/

> It really comes down to a contest, perhaps, between buyer and seller, a judgment of values according to the exigencies of the situation. There might be a time when a manufacturer might be loaded with some commodity and very desirous of selling it. We have had those experiences in the last year or two, where a manufacturer might want to get rid of what he had because

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236/ Testimony of F. H. Massman, Sumners Hearings 129.

237/ Sumners Hearings 107.

he needed the money. That is what is known as a buyer's market. On the other hand, we have periods of shortages. We have one today in pork. There is a seller's market.

The committee also had before it testimony that small retailers could achieve efficiency through vigorous price competition and collective buying, and that such increased efficiency would enable them to survive in competition with the large retailers. For example, the representative of a cooperative buying venture testified that when small retailers organize, they are able to secure every advantage available to the chain stores: 238/

Mr. Guyer: What advantage would a chain - store organization get over you?

Mr. Lazo: We are trying to say that they do not get any advantages that are not open to us. I think we are making a very good beginning.

In addition to cooperative buying, independents could, according to a retail grocer witness, engage in price competition with the chain stores. While meeting the chain store competition required the independent to use "loss leaders" and resulted in the independent's business being "bunched" on sale days, the results were not entirely adverse. 239/

238/ Utterback Hearings 318.

239/ Sumners Hearings 54. In fact, it was the independent grocer, not the chain, who first realized the single store efficiency of the supermarket. The large store, with its mass selling techniques, self service and cash and carry basis, reduced labor costs, and wide variety of merchandise, was first developed on the West Coast by independent grocers. Their success presented a very real threat to the chains, whose operation at that time consisted of a string of mom and pop stores under common ownership. It was only later, when the chains adopted the supermarket approach and some independent supermarkets expanded themselves into chains, that the supermarket, attacked by the supporters of the Robinson-Patman Act, became associated with the development of chain stores. Fulda, Food Distribution in the United States, The Struggle Between Independents and Chains, U. PA. L. REV. 1051, 1064-65 (1951).

The Chairman: Do you meet that [chain store] competition?

Mr. Pohlhaus: In many instances we do; in most instances I might say we do.

The Chairman: And you do it at a loss?

Mr. Pohlhaus: At a loss, and then endeavor, if possible, to come along with some of the other merchandise and make it up. But not having private brands, we cannot recoup that loss as quickly and easily as the corporate chains, who have private brands

Mr. Duffy of New York: On the close of the [sale] day's business, in relation to the net profit, is not that your most profitable day of the week?

Mr. Pohlhaus: It is the most profitable day of the week, sir, because there is the most business done on that day.

Finally, some witnesses made the point that if a small retailer refuses to adopt efficiency measures and declines to engage in vigorous price competition, consumer choice would operate to reduce his market share. Moreover, legislation attempting to prevent such a process would be unsuccessful. One witness, for example, while expressing a nostalgia for the small store similar to that expressed by pro-Robinson-Patman witnesses, argued that small retailers could remain viable only if they continued to serve a function for which the consuming public was willing to pay: 240/

> I would like to close by just one remark: I can recall, many years ago, when I was a very young boy, hearing my father say, 'A deadly thing has happened in our town. Someone has put in what they call a department store.' I said, 'What is that' He said, 'It is, in reality, in effect, putting under one roof a number of these stores that we are accustomed to going to.' He said, 'We must get the legislature to stop that, because, if we don't, all of these little stores that we now go to will be put out of business.' What is to save us from going to the department store? You had to go and buy from them, and you cannot change it. I can remember, as a very young boy, that made quite an impression on me, and I have recognized the economic development and I am wondering if the answer is not, the real answer is not that, so long as that one particular type of distribution continues to function and serve an economic purpose, that type of distribution will stay in business, just as the expensive hotel dining room will stay in business alongside of the cafeteria. I am wondering if it is not for the public to choose what type they wish and I am wondering whether the choice by the public will not eventually be made, irrespective of what laws may be passed in an endeavor to stop this economic evolution which is going on.

In addition to the testimony of various witnesses questioning the premise upon which the Robinson-Patman Act was based, Congress had before it the result

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240/ Utterback Hearings 489.

of an extensive study of the chain store phenomenon conducted by the FTC. As with the testimony before the Sumners and Utterback Committees, the FTC report made a number of points which, had they been fully appreciated at the time, would have pointed out the futility of any attempt to interfere legislatively with the development of new distributive channels.

The failure of Congress to appreciate fully the significance of the FTC report is understandable: it is apparent that the FTC itself did not, in all cases, base its final report and recommendations upon the statistics which it had gathered. For example, on the issue of the relationship of special discounts to lower chain prices, the FTC concluded "that lower selling prices are a very substantial, if not the chief, factor in the growth of chain-store merchandising, and that lower buying prices than are available to independents are a most substantial, if not the chief, factor in these lower selling prices." 241/ The actual statistics gathered by the FTC, however, make it clear that the chains' lower cost of goods sold was but a minor factor in the chains' ability to sell at a lower price. Based on a survey of four major cities, the FTC concluded that, of the difference in selling price between chains and independents, discounts of all sorts accounted for between three and thirty-five percent. 242/ Thus, if the price differential between a chain and independent outlet on a given item is one dollar, the elimination of all discounts would raise the chain's selling price by three to thirty-five cents; the chain store selling price would still be significantly lower than

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241/ 1935 FTC CHAIN STORE REPORT 53.

242/ *Id*. at 54-55.

that of the independent. A large portion of the price differential, the FTC found, was accounted for by the chain's ability to pass goods into the hands of consumers at a smaller gross margin and a smaller percentage of the sales price than could either the independents or the cooperative chains. 243/ This ability to charge lower prices was accounted for in large part by the chain practices of direct buying and vertical integration. The total gross margin for a consumer item purchased through an independent included not only the retailer's gross margin but also the gross margin of the wholesaler, broker, or other middleman from whom the independent purchased. In contrast, the chain stores made, on the average, 70 percent of all purchases direct from the manufacturer, 244/ permitting the manufacturer or the chain store to organize distribution in a more efficient manner.

The FTC study also emphasized that consumer choice, not predation, was the reason for the rapid increase in the chains' market share. In an FTC consumer survey, lower price was the most frequently cited reason for patronizi a chain store; moreover, the importance of lower chain prices and the tendency to purchase all consumer goods from the chain store outlets increased as the consumer's income went down. 245/

The FTC also conducted field interviews with many small town residents, precisely those consumers thought in Congress to be most hostile toward the chain stores. The objective results, however, showed sharply divided consumer

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243/ Id. at 67.

244/ S. DOC. No. 30, 72nd Cong., 1st Sess. viii (1932).

245/ S. DOC. No. 93, 73rd Cong., 2nd Sess. 52 (1934).

opinion on the merits of chain stores. A significant number of respondents living in small towns welcomed the coming of the chain stores into small town markets formerly dominated by independent retailers, as the following sample responses demonstrate: 246/

> County prosecuting attorney: In the last ten or fifteen years the town has changed a great deal. Formerly an agricultural center and a place for retired people to live, it became a dwelling place for a large number of miners working in the mines nearby. The miners want and need cheaper lines. The independents failed to meet this need. The chains put in the lines desired by the new element in town and are consequently getting the business.
>
> Mrs. F. B., proprietor -- Inn: Before the chains began doing business in the town, it was impossible to have an order for fresh vegetables filled unless the grocer was notified a week in advance. Now all that is changed. Fresh vegetables can be obtained at all seasons of the year at the chains.
>
> . . .
>
> Wife of the clerk of the circuit court: I trade with independents. Why? The answer can be summed up in one word -- politics.
>
> Mrs. B. -- occupation not given: Chain stores forced down the price of groceries. They are the balance wheel in price fixing. Were it not for the chain stores I don't know where the price of groceries would shoot up to.
>
> . . .
>
> Manufacturer: I notice that since the coming of the chains the local stores have pepped up and there is a noticeable improvement in their stores and stock.

246/ *Id.* at 68-73.

. . .

Newspaper editor: On the whole chains have helped the town. They are just better merchants than the independents. I think the bulk of the people sympathize with the independents, but they buy where they can get the most for their money.

. . .

Dining room proprietor: Though I would like to support the home merchants, I favor the chains, as I was here and know how the townspeople were scorched by high prices before the coming of the chains.

Attorney: Since the coming of the chain stores there has been an improvement in the commercial atmosphere of this town. Merchants have brushed up their places of business and improved their methods of doing business. There is more efficiency in store management than there was formerly. The business district has improved in appearance. I am not advocating the cause of the chain stores, but I must confess to the facts as I see them. There seems to be a more energetic spirit displayed by merchants and they are more expert at merchandising.

Physician: The coming of the chain stores reduced my grocery bill. When the chain stores came here there was a great deal of agitation against them, but I do not hear so much said against them now. The chains have placed the independent grocery store on a higher plane. Of course, some of the small-fry grocers have been weeded out. Now, then, let us look at the matter from an unbiased point of view. The chain stores employ people. They pay wages. The managers at least have families and they rent homes. If they are taken sick, they employ a physician. They spend money in many ways. The chain stores have enlarged the trade territory of this city. The evidence is found in the large number of people who come here to trade on Saturday night. Our streets are lined with automobiles. It was not like that before the chain stores came here. These people who come here Saturday night do not spend all their money in chain stores, either. Other merchants are patronized.

School superintendent: In my opinion the chain store is a good thing. It acts as a safety valve. It keeps the independents from holding us up. I like to see every tub stand on its own bottom. If the chains can sell

> merchandise cheaper I will have some money left to spend for something else. Six years ago there wasn't a decent grocery store in the town. The chains came in and the independents cleaned up their stores. The chains are paying taxes through the medium of rent and thus they support the schools.
>
> Bank cashier: Some of the grocery stores may be feeling the effect of chains, but it is partly their own fault. The day of the dirty, ill-kept grocery and food store is past. The people will not trade in it, especially when the chain prices are lower and a fuller selection of merchandise is offered.

The FTC study also cast doubt upon the widely held assumption that the chain stores' success was due in large part to the frequent use of "loss leaders," the practice of selling an item below cost in order to entice customers into the store. The FTC found that the use of lead items in order to boost sales was, in fact, common but that true below-cost sales were much less frequent than formerly believed. The Commission found that, for the year 1928, only 11.9 percent of the chain stores responding to the study actually employed the loss leader device. 247/

Finally, the FTC chain store study cast serious doubt on the assumption that the chain stores would, absent legislation, monopolize the retail market, and then raise prices once the independents were eliminated. The conclusion reached by the FTC was, in fact, very much to the contrary. 248/

247/ S. DOC. No. 51, 72nd Cong., 1st Sess. 20 (1932).

248/ 1935 FTC CHAIN STORE REPORT 19.

> In the grocery group, where chain-store systems have reached their largest development, it has been shown that the large national and sectional chains participate proportionately with smaller sectional and local chains in retail grocery sales falling to these types. The competition which they furnish to each other, supplemented by that of independent stores, would seem to negative monopoly by any individual chain. The same is true as to the larger chains in the drug group, where the two large national chains in active competition with each other at various points together control but 6.8 percent of total retail drug sales.
>
> A study of the extent to which chain-store companies have invaded the general field of retail distribution of commodities does not indicate a monopolization of that field, taken as a whole. For the year 1929 total chain-store sales represented 19.3 percent of the aggregate retail sales of the United States as against 80.7 percent for all other methods of distribution. Local chains accounted, however, for 6.7 percent and sectional chain companies only 12.6 percent of the United States aggregate sales.

It should be noted that the above information adverse to the premises of the Robinson-Patman Act did not go entirely unnoticed. Representative Celler of New York prepared a minority report for the Committee on the Judiciary summarizing the arguments against the passage of Robinson-Patman. 249/ The minority report made a number of points: that the Bill was an attempt to deter the development of more efficient manners of distribution by protecting the traditional 3-tier system; that the very device by which independent retailers might compete, the formation of voluntary chains, was hindered by the Bill; that there was little, if any, danger of monopoly in the retailing field; that quantity discounts were usually justified and accounted for only a small portion of the chain stores' lower selling price; and that the ultimate result of the proposed legislation would be increased prices to the consumer.

249/ H.R. Rep. No. 2287, pt. 2, 74th Cong., 2d Sess (1936).

A number of conclusions can be drawn from the legislative history of the Robinson-Patman Act. Much of the support for the Act came from those who had a special interest in maintaining traditional forms of distribution: the wholesaler or other middleman and the independent retailer to whom he distributed. Their explicit request for protection coincided with the pressure created by the depression, leading Congress to believe that that protection of the wholesaler and the retailer was consistent with the public interest in preserving time-honored values: independence, self-reliance, dispersion of power, and familiar social structures. Chain stores were viewed as part of a general process which would lead to the destruction of the public good as traditionally understood. In economic terms it was felt that the statute would provide a substantial service by preventing a tendency toward concentration and monopoly which, in the long run, would leave the consumer, already ravaged by the depression, helpless in the face of the impersonal monopolist.

In the emotionally-charged climate, it is not surprising that the hearings and debate failed to produce the kind of calm, well-reasoned analysis which the nature of the problem and the scope of the proposed remedy required. The contrast between what occurred in 1936 and the attention to solid economic analysis which Congress now demands was highlighted by a Review Group witness. 250/

> Congress held very few hearings, considering the sweeping nature of the legislation. The House Committee held a short set of hearings on the original Patman Bill in the early summer of 1935; a few more days in February, 1936. Meanwhile the Senate Committee held no hearings

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250/ Prepared Statement of Donald I. Baker at 15-16, DCRG Hearings.

> on the Robinson Bill and only two days of hearings on the Borah-Van Nuys Bill in March, 1936. That was pretty much the extent of the record developed by the Congress.
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> We might contrast this sparse legislative process with what Congress itself did last year--and for several years previously--before it decided to overhaul the rules governing competition in the securities industry. The House Committee piled up ten volumes of hearings on pricing, market access, and related competitive questions; and the Senate Committee added almost as many. They weighed and reprinted vast amounts of material; and then each committee did a thorough industry study recommending legislation. Ultimately, the Congress decided, based on these studies, that the protectionist price-fixing should be eliminated--over the emotional claims of those protected that this would lead to "cut-throat pricing," "predation," and "monopoly". Congress may or may not turn out to be absolutely right on every key point in the 1975 securities reform legislation--but where it turns out to be wrong this will not spring from a lack of concern about facts.

More significant than the failure to investigate thoroughly was a second error: an extensive factual records which cast doubt on central assumptions underlying Robinson-Patman was ignored in favor of emotionally tinged pleas for help and untested economic assumptions. Congress disregarded the FTC's chain store study which forewarned that any statute which operated to control only a firm's cost of goods sold would be but marginally effective in protecting a specific segment of the economy, if success were to be measured by the continued existence of specific competitors. Congress also accepted anecdotes of alleged predatory practices over the Commission's evidence indicating that discounts extracted from suppliers and lower prices to consumers were both non-predatory and economically justified. Finally, the use of straight line projections to predict the expected monopoly power of chains was fraught with risk. The FTC study much more clearly stated the facts with respect to this issue.

D. Current Justification for Retaining the Robinson-Patman Act

Current justification for the Act has been elicited by a number of recent studies on the effects of Robinson-Patman. Two investigations of the antitrust laws, the Neal and Stigler reports, 251/ raised doubts about Robinson-Patman's consistency with the policies in favor of competition embodied in the antitrust laws. Those reports triggered Congressional response in the form of a special subcommittee to study small business and the Robinson-Patman Act. 252/

The most recent round of debate on the statute began with two Department of Justice draft proposals for reform of the Act, which were circulated in 1975 for the purpose of eliciting comments. As occurred in response to the Neal and Stigler reports, the House Small Business Committee established a special subcommittee, the Ad Hoc Subcommittee on Antitrust, The Robinson-Patman Act, and Related Matters, to respond to the proposals.

During December of 1975, hearings were held before the Domestic Council Review Group to gather facts about the effects of the Robinson-Patman Act, to consider proposals for change and to provide a forum for public response to the Department of Justice proposals.

Testimony given before the Domestic Council Review Group and the House Subcommittee reveals a number of common themes in the defense of Robinson-Patman.

251/ White House Task Force Report on Antitrust Policy (1968) (the Neal Report); The President's Task Force Report on Productivity and Competition (1969) (the Stigler Report).

252/ Hearings on Small Business and the Robinson-Patman Act Before the Special Subcommittee on Small Business of the House of Representatives, 91st Cong., 2d Sess. (1970).

1. Protection of Competitors

Protectionism remains an explicit goal of some supporters. 253/

> This law [the Robinson-Patman Act] has stood the test of time. It has repeatedly been attacked and after each encounter with its detractors, this statute has emerged stronger than ever, and it still stands as solid as the Rock of Gibraltar--a bulwark of protection for the 9 1/2 million small entrepreneurs of this great Nation of ours.
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> *   *   *
>
> Mr. Gonzalez: Mr. Chairman, I might ask a question. I certainly agree with you. I think the small businessman, as Dr. Webb, Prescott Webb defined it as a fellow who wasn't able to get a lobbyist in his behalf in Washington. The small businessman certainly needs congressional oversight, continuous congressional oversight and protection. I think that he is an endangered species... 254/

As has been shown, the Robinson-Patman Act was passed at a time when a number of factors combined to make protectionist regulation, rather than competition, seem a reasonable course for national economic policy. In the present, when public debate is focused on ways to untangle the web of regulatory legislation of that period, it is not surprising that those who would retain the Act attempt to disassociate Robinson-Patman from other depression-era legislation, such as the fair trade laws. Counsel for the National Small Business Association, in his testimony before the Review Group, made just such an attempt. 255/

253/ Testimony of Rep. Patman, Subcommittee Hearings, pt. 1 at 7.

254/ Id. at 13.

255/ Testimony of Thomas A. Rothwell, DCRG Hearings, Tr. 455.

> The McGuire Act, anybody who asks or tries to compare McGuire and Robinson-Patman is either ingenuous or, as I said, an over-zealous advocate.

Any such assertion, however, must be weighed not only against the evidence of similar purpose contained in the legislative history, but against the admission of similar purpose expressed by that same organization in its defense of the recently repealed fair trade legislation. 256/

> Today there are only two statutes in our antitrust code that give any protection to small business against the unfair competition of giants. These are the Fair Trade laws and the Robinson-Patman Act.

2. Maintenance of Equal Competitive Opportunity for Small Businessmen

Support for the Act would continue regardless of the legislation's ability to protect small business interests. Without conceding that the Act may be unable to insure the survival of small business, supporters point out that it may nevertheless have the salutary effect of giving a psychological boost to the small businessman faced with competition from larger rivals. Its supporters argue that the existence of the statute may, in many cases, provide the encouragement which is needed if a small businessman is to enter into or remain in the admittedly hazardous occupation of retailing. In response to a question concerning the net benefit of the Act, one Review Group witness testified: 257/

> There is a net benefit that a man who is struggling in business and looks to the Government for help is going to survive. In essence, that is what we are talking

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256/ Prepared statement of the National Small Business Association, Hearings on H.R. 2384 Before the Subcommittee on Monopolies and Commercial Law of the Committee on the Judiciary House of Representatives, 94th Cong., 1st Sess. 153 (1975).

257/ Testimony of Philip O. Friedlander, DCRG Hearings, Tr. 436.

about, at least our group is.

> He may be only one guy employing twenty-five people, but when he's got a problem, he has no place else to go except to get an enforcement under the current statutes, and that is what we are objecting to because they are not being enforced even when the dealer comes to Washington, takes the risk and comes down here and nothing happens.

Similarly, one witness before the 1975 House Hearings testified that the Robinson-Patman Act has the beneficial effect of promising small firms that the federal government is enforcing fairness in the marketplace, giving the small businessman the psychological boost which may be needed to motivate him to enter into or remain in the marketplace. 258/

> The survey documents another quasi-sociological aspect, the value of Robinson-Patman enforcement in improving morale of small buyers and encouraging them to assert themselves in bargaining. Even in markets where handicaps do not exist, small buyers might be demoralized by the feeling of unjust handicaps in bargaining, were it not for the reassurance provided by the presence of Robinson-Patman enforcement. This demoralization itself might substantially contribute to socially disfunctional declines in the offerings of the many varieties and variations to be found among small firms, when it is often to these very firms that we must look for innovation and provision of varieties and variations in product and service alternatives.

Robinson-Patman Act supporters urge that the small businessman is as efficient as the large, and needs only an equal opportunity to compete with large companies. For example, one small business representative testifying before the Review Group quoted from a study of the food distribution industry: 259/

258/ Testimony of Robert C. Brooks, Jr., Subcommittee Hearings, pt. 1 at 429.

259/ Testimony of Donald A. Frederick, DCRG Hearings, Tr. 378.

> We have been sold a bill of goods. Smallness may appear inefficient when put beside a model of perfect efficiency, but that model exists only in the minds of economists. In the real world, efficiency and competitiveness are products of economic smallness. Compared with the performance of giantism, smallness looks awfully efficient.

Given the equal opportunity to compete, and the chance to demonstrate the efficiency of small business, the small firm needs but a statutory version of the golden rule. This need, according to a well respected antitrust attorney and author testifying in the Subcommittee Hearings, is supplied by the statute in its present version, provided it is vigorously enforced. 260/

> Mr. Kintner: And yet, the Robinson-Patman Act basically provides for equality of opportunity among competing customers or purchasers of a product. There is nothing particularly obtuse about that; it is a very simple moral code, in my opinion, that people should be treated fairly. In the same way that we have a requirement of equality before the law, the small businessman ought to be able to start the race with his bigger competitor on a basis of equality.
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> * * *
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> Mr. MacIntyre: Now, speaking of the Robinson-Patman Act--and I am referring back now to a statement you made on page 7 of your statement in which you referred to the "expression of the intent of Congress was to restore as far as possible equality of opportunity in business by strengthening the antitrust laws and protecting trade and commerce against unfair trade practices and unlawful price discrimination."
>
> I would like to refer again to that phrase and that quotation, "equality of opportunity." It is your view, as I judge it from your statement, that the Robinson-Patman Act was designed to provide that; not to really protect people against competition, but to provide an equality of opportunity at the starting point. 261/

260/ Testimony of Earl W. Kintner, Subcommittee Hearings, pt. 1 at 260.

261/ Remarks of Everette MacIntyre, Subcommittee Hearings, pt. 1 at 262.

> Mr. Kintner: Absolutely. There is no purpose in the Robinson-Patman Act to protect the inefficient, ineffectual businessman, large or small, but only to provide businesses with equality of opportunity so that they can start the race, the competitive race, on some basis of equality. 262/

The equity argument is also advanced as the foundation for a corrollary argument: if a seller is compelled to grant the same price to all purchasers, the net effect will be lowered prices to all purchasers. 263/

> A manufacturer may and does set his own price. What we say is make that price available to all. Do not favor large over small customers (unless truly justified by cost savings); do not favor one customer over another. If the manufacturer sells at his lowest reasonable price, then all consumers will benefit through price competition of healthy, vigorous dealers. Independent dealers know how to compete and they are doing so successfully.

3. Prevention of Monopoly in Distribution

The most important current argument advanced in support of the Act is that it forestalls monopoly in distribution. Proponents of Robinson-Patman state that, if the Act is repealed, large firms would engage in predatory conduct to drive many small firms from the marketplace. The long run effect would be increased concentration in the marketplace and a tendency, once competition from small business is reduced, toward higher prices for the consumer. One Congressman described the process during the 1975 House Hearings. 264/

> [Y]ou see this happening throughout America where that independent is being driven out of business. Yes, the biggie comes on and offers, you know, a relatively low price or whatever goodies it offers,

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262/ Testimony of Earl W. Kintner, Subcommittee Hearings, pt. 1 at 262.

263/ Testimony of Philip O. Friedlander, Jr., DCRG Hearings, Tr. 387.

264/ Remarks of Rep. Hanley, Subcommittee Hearings, pt. 1 at 27.

> that the independent cannot possibly offer. Once the biggie kills the independent then it has got the marketplace to its own and then it can do whatever it wants.

The consumer is best served, according to this analysis, by a marketplace made up of numerous small competitors. The goal of the antitrust laws ought to be to create and maintain such a marketplace. The Robinson-Patman Act, therefore, is a necessary device to assure that as many firms as possible remain in the market. Protecting specific firms is merely a means to a socially desirable end, the protection of competition.

The small business community's belief in the potential for predatory or systematically discriminatory conduct on the part of large business is demonstrably deep-seated. 265/

> Large corporate interests engaged in the retail field will use brute economic power to extract preferential prices from their suppliers. The results will be unfair competition between large and small retailers with the eventual demise of the latter.
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> * * *
>
> If the retail drug field is characteristic of the effect of the repeal of this Act, the result will be the wholesale demise of independent businessmen and the rapid demise of the independent retail pharmacies, in both urban and rural areas. The end result in many areas will be a monopoly situation controlled by some large out-of-state corporate chain drugstore, little concerned with serving the community except to the extent it has a positive effect on their corporate ledger.

265/ Testimony of William E. Woods, DCRG Hearings, Tr. 401, 403.

It is, of course, these predictions of monopoly in the future which the Act's supporters argue justify the use of the incipiency standard which has caused the courts and businessmen so many problems. 266/

> Mr. Kintner: [Y]ou would not have to think in terms of dismantling big business if you protected competition and prior to that time picked up these violations in their incipient stages rather than waiting for them to become full-blown monopolistic practices. And that was the purpose of the Federal Trade Commission when it was established. It was a congressional purpose in establishing a trade commission, as you, Mr. MacIntyre, well know and have said so many times.

Those who believe firmly in the Robinson-Patman Act argue that, whatever the benefits of increased price competition gained by the repeal of the Robinson-Patman Act, in the long run the demise of the small businessman, and the subsequent monopolization by big business interests would lead to decreased consumer choice and the use of monopoly pricing by the surviving firms. 267/

> We cannot allow RP to be repealed. That could emasculate our industry and reduce competition. Many smalls, we don't know the number, might not survive, and of course consumer buying choices would be reduced owing to fewer stores.

The Robinson-Patman Act proponents argue that, once monopoly or near monopoly has been achieved, the benefits of any price competition encouraged by repeal of the Act will prove illusory. 268/

266/ Subcommittee Hearings, pt. 1 at 262.

267/ Testimony of Douglas Wiegand, DCRG Hearings, Tr. 398.

268/ Testimony of William E. Woods, DCRG Hearings, Tr. 401-402.

> Gentlemen, I submit if this is repealed it will hurt more than the small businessman. The consumer is going to suffer enormously if you don't start enforcing the Robinson-Patman Act or if you continue attempts to repeal the Act.
>
> When the monopoly is complete and the independent service-oriented drug store is driven out of business, whether you believe it or not you may be sure that the consumer will start paying higher prices throughout this land.

The real beneficiaries of any tampering with the statute, its proponents argue, will be the shareholder of the large, monopolistic concern, rather than the consumer. 269/

> When the large non pharmicist-owned chain drug corporations become the monopolists of the prescription dispensing in this country, I ask this group whether supposed cost savings, in your opinion, will be distributed to the consumer or to the stockholders. I think you can answer that yourselves.

Thus, current justifications for Robinson-Patman are quite similar to those offered during preceding debates: protectionism, equality of opportunity, and the prevention of concentration.

269/ *Id.*, at 403-404.

Chapter IV. AN EVALUATION OF THE ECONOMIC AND POLICY ASSUMPTIONS UNDERLYING ROBINSON-PATMAN

Chapter III of this Report describes the enactment of Robinson-Patman as the product of the emotions created by the emergence of new methods of distributing consumer goods, particularly chain store distribution, and by the economic trauma of the depression which caused severe concern on the part of businessmen and public officials about the future of small business. As shown, the purpose of Robinson-Patman was to protect small business, to establish "fairness" in inter-business pricing, to prevent predation, and to forestall increases in industry concentration. This chapter of the Report will first analyze the economic assumptions that underlie Robinson-Patman and then address the Act's goals -- considered by some to be just as valid today as in 1936 -- in order to determine whether the benefits to the public interest which can be achieved by Robinson-Patman outweigh the costs that the Act imposes.

A. The Robinson-Patman Act is Based on Questionable Economic Assumptions Prevalent in the 1930s

In order to intelligently understand the impact of any government intervention in the marketplace, one must first understand the assumptions upon which that intervention is based. Otherwise one may attribute certain adverse effects of a regulatory statute to poor drafting or to improper statutory interpretation and administration when in fact, these effects are in harmony with the goals which the Act's sponsors meant to adopt. An attempt to rework the language of the statute or to improve the "quality" of the decisions made by those with the responsibility to enforce the law similarly may not be wholly successful insofar as the very nature of the statute itself is in conflict with the forces that guide pro-competitive business behavior.

In drafting Robinson-Patman, the Act's sponsors appeared to make several assumptions about economic activity. These assumptions, dealing with the appropriate direction of prices -- up or down -- the manner in which prices are set, the role of costs in the determination of process, and the extent of predatory pricing, were understandable in light of the conditions of the 1930's. Some of these assumptions were explicitly stated before Congress. Others are implicit in the logic of a price discrimination statute. They are, though, not supported by careful observation of present business conditions.

1. <u>The Assumption That Prices Should be Uniformly Higher</u>

The first assumption made by drafters of Robinson-Patman was that the general level of prices should be higher. This assumption is inherent in the Act's structure: businessmen need <u>not</u> decrease their price to particular customers if costs or market conditions change in particular areas; to the contrary, businessmen fall under Robinson-Patman scrutiny and prohibitions when such decreases are made. This structure reflects the central concern of the Act's sponsors that firms would grant special discounts off list prices, or give allowances which would reduce the price charged to a competitor, or would otherwise charge prices at levels which were "too low."

In the midst of the current national debate on how to reduce the rate of inflation and to stabilize the cost of living, the extraordinary concern expressed by the authors of Robinson-Patman with any action which serves to reduce prices may be difficult to comprehend. To a lawmaker in the 1930's, however, the world was quite different. The country was in the midst of the great depression and was experiencing a period of serious deflation. 270/ As was demonstrated in the previous discussion of the history of Robinson-Patman, lawmakers such as Representative Patman were concerned that paying low prices for commodities would decrease the wages of farmers and workers and thus prevent national prosperity from reemerging. 271/ As one witness before the Review Group's hearings testified, it was a central tenet of the New Deal administration from 1932-1936 that prices should be higher. A reason for this was the erroneous belief of at least one cabinet member that "if prices could only be made to go up by what ever means necessary, that employment levels would be restored." 272/ This belief is also reflected in other legislation enacted during the same period: for example, the Motor Carrier Act of 1935 and the Civil Aeronautics Act of 1938, both of which respectively established minimum rate regulation in the trucking and airline industries respectively.

Most importantly, the Act followed even broader legislation designed to accomplish the same purpose. The Robinson-Patman Act was introduced soon after the decision of the Supreme Court holding that the National Recovery Administration (NRA) and the "Codes of Fair Competition" promulgated thereunder

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270/ The Consumer Price Index (1958 = 100) fell from a value of 59.7 in 1929 to a low of 45.1 in 1933. By 1939 the index had risen to only 48.4. AT the same time, the unemployment rate rose from 3.2 percent in 1929 to 24.9 percent in 1933 and was 17.2 percent in 1939. ECONOMIC REPORT OF THE PRESIDENT, 1967, Table B-42, B-20.

271/ 80 CONG. REC. 8113 (1936) (Remarks of Rep. Patman); Prepared Statement of Donald I. Baker, DCRG Hearings 13-14.

272/ Testimony of William F. Baxter, DCRG Hearings, Tr. 38.

were unconstitutional. 273/ As a Presidentially-appointed study commission noted, a major purpose of the NRA was to ensure "improved earnings of business." 274/ Under the various NRA codes businesses established minimum price levels; they required the filing of prices, a procedure which had as its purpose in part "the reduction of competitive pressures on prices with consequent higher prices reached without collusion, [and] possibly also the facilitating of actual understandings on prices," 275/ and the codes also regulated other trade practices dealing with allowances and similar forms of price concessions. Not surprisingly, the "natural tendency of the NRA was to raise the prices of manufactured goods and of goods sold at retail in general." 276/ The Act was a key element of a series of programs designed to "put an end to the vicious downward spiral that had brought the country to the verge of real disaster by the Spring of 1933." 277/ Hence, insofar as Robinson-Patman, which incorporates some NRA code provisions, acts to eliminate or moderate the competition or to increase prices, "it is not a failure in terms of its authors. It is a

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273/ A. L. A. Schechter Poultry Corp. v. United States, 295 U.S. 495 (1935).

274/ COMMITTEE OF INDUSTRIAL ANALYSIS, REPORT ON THE OPERATION OF THE NATIONAL RECOVERY ADMINISTRATION, H. R. DOC. No. 158, 75th Cong., 1st Sess. 7 (1937).

275/ Id. at 144.

276/ Id. at 7-8.

277/ Id.

great success." 278/ Of course, the assumption that high prices would bring high employment has been proved demonstrably false by events of today.

2. The Assumption That Manufacturers Need To Subsidize Price Reductions For Some Buyers By Price Increases For Others

The Act is also based on an erroneous assumption about the way in which prices are set. In the ideal world, as seen by Robinson-Patman proponents, prices to all customers would be the same. Any deviation from that uniform price would occur only if the cost of serving a particular customer differed in an exact amount by the deviation from the list price. Whether such a model had any relationship whatever to the manner in which prices are set in an advanced industrial economy was never questioned by the proponents of the Act. That they should have believed this to be the case is not, however, surprising, for the Act was initially drafted and supported in large part by retail and wholesale grocers. These are industries traditionally characterized by high turnovers and low margins. Sales prices, for the most part, reflect the cost of goods purchased plus "rule of thumb" markups for particular types of items. In industries, then, where unit pricesfor goods sold were in the tens of cents, a three or four percent discount may have seemed unreasonable unless justified, if at all, by extraordinary circumstances.

But Robinson-Patman is not limited to the grocery business. Rather, it is a statute of general applicability and its assumptions must be as broadly valid as its coverage. An examination of pricing in real world

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278/ Testimony of William F. Baxter, DCRG Hearings, Tr. 39.

domestic markets shows that prices are set not by just the cost of producing goods (the supply side of the equation) but by the interaction of supply and demand. Even in the theoretical world of perfect competition, with large numbers of buyers and sellers, prices need not necessarily be uniform. If markets are segmented geographically, for instance, different demand conditions may result in different prices in different markets.

In addition, the price setting process in the real world is much more complex than in a world of perfect competition, which requires, aside from large numbers of buyers and sellers, perfect knowledge among all parties of market conditions, and most importantly, an open market place for the setting of prices. In the "workably competitive" markets that characterize most of our economy, there are fewer buyers and sellers than in the model of perfect competition. Prices are often set in direct negotiations between purchaser and supplier. Firms are of differing relative sizes and efficiencies, and possess varying degrees of entrepreneurial skill and knowledge about market conditions. Consequently, in the world of workable competition -- the environment in which Robinson-Patman will most frequently have its impact -- prices will depend on the relative bargaining skills and positions of parties, the relative demand characteristics for each buyer, the existence of alternative suppliers for a buyer, or his ability to manufacture a product if he does not receive a satisfactory price quote. Under these conditions, a variation in the ultimate prices charged to individual customers is to be expected. Moreover, any public policy dealing with pricing must take into consideration the fact that under present market conditions, price discrimination must play an integral role in the competitive process.

The sponsors of Robinson-Patman, concerned with maintaining price parity among buyers rather than price competition among sellers, viewed the bargaining process through a distorted lens: they saw discriminatory prices only in terms of large-buyer power and not in terms of the market power of the seller which permitted him to charge discriminatory prices. Consequently, they thought that the "loss" to sellers from the lower prices to the larger buyers would have to be "subsidized" by higher prices to smaller buyers. 279/

It is apparent, upon reflection, that this is not the case. Where the seller has enough market power to successfully maintain a higher price to disfavored purchasers (*i.e.*, no competitors exist to undercut it), the seller can always charge the higher price and need not rely on the "excuse" of lower prices in sales to a favored customer. That is, if the seller can "get away with" charging higher prices to smaller purchasers there is no reason he should refrain from doing so until he receives a request from a larger customer for a price concession.

Businesses with market power can generally be expected to charge a "profit maximizing" price. Depending on the relative elasticities of demand (the proportion by which purchases will change in response to a given change in price) for sales to various classes of purchasers, the profit maximizing price charged by a seller with market power may be different for retailers of differing sizes and types, even when these purchasers do not exercise market power of their own. Where sellers are

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279/ See text at page 124, *supra*.

already charging profit maximizing prices and a purchaser exercises his market power so as to force the manufacturer to lower his price, the seller will not necessarily increase his profits by raising its prices to his other purchasers. If purchasers are in competition with each other, the chief area of Robinson-Patman concern, customers will be drawn by the price differential from the disfavored firm to the favored buyer. Any attempt by the seller to raise the price charged to the disfavored buyer will likely induce more customers to go to the favored retailer. The discriminating manufacturer will thus increase its sales at the lower price charged to the favored customer and decrease its sales at the higher price charged to the disfavored ones. Depending on the relative elasticities of demand and the extent to which the favored and disfavored buyers are really in competition for the same customers, the seller may thus lose money by increasing his prices to the disfavored purchaser.

3. The Assumption That Discriminations Uniformly Favor Larger Buyers And Never Result In Lower Prices Throughout The Market

The supporters of Robinson-Patman also assumed that larger buyers receive price concessions which are never reflected in lower prices to other purchasers. Again, this belief fails to take into consideration the existence of oligopoly pricing power on the sellers' side. In many cases pricing discrimination is actually part of a dynamic process by which excessive price levels in oligopoly industries are brought down toward a more competitive level. 280/ In oligopolies, list prices tend to

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280/ See discussion of countervailing power and pricing flexibility at pages 47-58 , *supra*.

be "sticky," there being little incentive for a supplier to change his list price. The only incentive for a price decrease would come from the eagerness of a manufacturer to gain a large customer, or to retain a customer in the face of a lower price quote from a competitor or a threat by the customer to produce the product himself by vertical integration. The process was explained by a Review Group witness: 281/

> The prototype situation on which the secondary line cases come to bear is one that has the following basic characteristics: There is some group of sellers, and they have some degree of market power. Prices exceed marginal costs, at least short run marginal costs, and this fact gives rise to the occasion for significant price differences.
>
> The Sherman Act keeps the sellers from getting together and explicitly fixing prices and prohibits their communicating about prices. They will have doubt, each in his mind, what others are selling for, and to whom they are selling at what price.
>
> When a seller hungry for business decides to make a price concession, to whom will he make a concession? Almost inevitably to effect the large sale. There is more payoff in it, and therefore it is more likely than not that the first beneficiary of a break from the prevailing prices in such an industry will be to a large buyer.
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> Assuming that Seller No. 1 has gained a large buyer, someone has lost a good customer, and in that sense now has excess capacity and has to go looking for some other buyer. So, the pressures are magnified for another price concession.
>
> Indeed, to the extent he finds out how he lost this good customer, the second seller is motivated for a variety of reasons to respond in kind, and perhaps attack a large customer of the first seller. And the process is typically generalized until these off list prices filter down through most of the retail categories. Perhaps ultimately the industry rationalizes its pricing process by printing new list prices which reflect the now somewhat lower level of prices and more nearly reflecting real cost.

281/ Testimony of William F. Baxter, DCRG Hearings, Tr. 41-43.

Inflation of course may be disguised in this process largely, but historically real costs of most commodities do come down, and then the whole process may start again. It is a very healthy process; at least it is healthier than the alternatives.

It would be nice of course if we could somehow maintain a world in which there were no manufacturers's markets in which sellers had any market power at all; but since that is in fact impossible, it is highly desirable that this process of covert price concession, which is gradually generalized among this set of customers, and ultimately rationalized in the form of a new price list, with the process all then starting over.

Professor Robert Brooks, an economist who studied the effects of several Robinson-Patman orders on behalf of the Federal Trade Commission made clear that the failure to distinguish between sporadic and systematic price discrimination may lead to anticompetitive actions on the part of public policymakers. Thus, he was opposed to enforcement of the Robinson-Patman Act directed at "sporadic, unsystematic discrimination which is part of healthy competition." 282/

A former chairman of the Federal Trade Commission , however, testifying before the Review Group noted that Robinson-Patman is not confined to prohibiting systematic discrimination: 283/

Mr. Flexner: Assuming that he's [Professor Brooks] talking about the secondary line situation, would you agree with that as a standard in secondary line cases, that the discrimination should be systematic before it should be attacked as a violation?

Mr. Kintner: No, because the Robinson-Patman Act not only gets at systematic price discrimination, but it gets at individual price discrimination, and I think that is very important.

282/ Testimony of Robert C. Brooks, Subcommittee Hearings, pt. 1 at 429.

283/ Testimony of Earl Kintner, DCRG Hearings, Tr. 180

4. The Assumption That Price Differentials Should Primarily, If Not Exclusively, Occur As A Result Of Different Costs

The next faulty assumption underlying the Robinson-Patman Act is that costs are the sole determinant of prices. In the real world, companies face a variety of fixed costs, such as debt service or depreciation, research and development expense, and many forms of advertising, which do not vary with the amount of the commodity produced. In producing particular goods they also incur joint costs, such as general corporate overhead, and the cost of purchasing raw materials (such as crude oil) which may vary according to the total output of an industry, but which cannot be assigned to any one product line.

Most economists agree that the relevant price setting costs are the "marginal" costs of producing a particular good. By pricing on the basis of marginal costs, goods can be produced in a manner which makes the most efficient use of society's resources because the cost of goods is related to the expenses incurred in actually producing those goods. Economists find, moreover, that there is no correct way of allocating joint and fixed costs. Under some circumstances, the most efficient way to cover those costs by sales prices is to allocate them according to the relative demand characteristics of each market, *i.e.*, allocating those costs to customers who are more willing to pay for them. Additionally, in times of slack demand when there is an excess of productive capacity the total revenue from the sale of a product may not be able to cover the fixed or joint costs involved in its production. In such cases, it is desirable that a manufacturer avoid bankruptcy or other financial difficulties by pricing goods in a manner which would help him minimize his total corporate loss.

All of this means, therefore, that in a complex industrial society like ours, where industries are not in a perfect state of equilibrium of demand and of productive capacity, one would expect some discrimination among different customers and different geographical areas. Such discrimination would prevail even though there is absolutely no desire on the part of any buyer to achieve a monopoly in a particular market or to drive competitors out of business. Such non-systematic discrimination is both rational and desirable from the standpoint of the health of individual firms and the consuming public.

In the real world, the competitive businessman is always seeking out new business and new customers. When faced with the opportunity of making a sale, the competitive businessman basically asks himself one question: "Can I make money on this transaction?" In negotiating the price for the transaction, the ordinary businessman is not concerned with, nor does he really know, whether the sale in question would cover what an accountant would determine to be the fully allocated or joint cost of the transaction. While he knows that all his company's sales revenue must cover all its costs, for any particular transaction his company need only receive more additional revenue than it will incur additional expenses.

Furthermore, the only cost information which a businessman usually has is that for the prior accounting period. In today's inflationary economy, he may only be able to guess at his future costs of production or inventory replacement. In deciding what price to offer under such uncertain conditions, the businessman must also consider whether the proposed purchase will be of sufficient volume to allow him to increase production capacity or to take the risk of signing a long-term supply contract at perhaps a lesser price to him. But the decision to make the sale at a given price is really, to the businessman, a short-run proposition. 284/ If the businessman hesitates too long in order to make detailed analyses of the effect of a particular transaction on his long-run financial prospects, he may find the prospective purchaser has left for another supplier more ready to meet his immediate needs. As one commentator has noted: 285/

> Contrary to an important legal premise of the Robinson-Patman Act, price variations are not causally based on costs, but on the interplay of manifold economic pressures . . . . Indeed, prices -- which influence sales, hence production volume, which in turn governs the efficiency of the firm's plant utilization -- may determine the unit cost of the ultimate output more directly than vice versa.

Similarly: 286/

> [T]he illegal prices with which the Robinson-Patman Act deals are short run; the law mistakingly attempts to apply to such prices a long run basis of price determination [i.e., costs] . . . . The cost theory of pricing which underlies some parts of the act is antediluvian. Neither in theory nor in practice does cost have the price-making role assigned to them under this law. It is not surprising, therefore, that the attempt to use this archaic approach to pricing has been accompanied by such a bewildering number of difficulties.

284/ The possible exception is the signing of a long-term supply cost contract.

285/ F. ROWE, PRICE DISCRIMINATION UNDER THE ROBINSON-PATMAN ACT 31 (1962).

286/ Backman, An Economist Looks at the Robinson-Patman Act, 17 A.B.A ANTITRUST SECTION REP., 343, 347 (1960).

The hallmark of the successful businessman is the way in which he responds to the short-run pressures governing the relationship between his company, his suppliers, and his customers, while at the same time assuring his firm's long-term financial success. In a freely competitive situation, the businessman has the flexibility needed to cope with the dynamic forces of the market place. A statute like the Robinson-Patman Act, which fails to reinforce such flexibility, necessarily limits the ability of businessmen to utilize their skill as entrepreneurs.

5. The Assumption That Prices Are Set on a Spot Market Rather Than Long-Term Basis

The sponsors of Robinson-Patman assumed that prices for large and small buyers are set at the same time and may be compared as contemporaneous transactions for the purpose of determining the existence of a discount. Such a perception is again consistent with the fact that the Act's major beneficiaries, wholesalers and retailers in the food and drug trades, were businesses which bought at non-negotiated list prices or current market prices.

In the more complex economic relationships of today's economy, particularly in transactions between large organizations, goods may be purchased under long-term contracts. Such contracts may contain various escalator clauses relating to certain inflation rates 287/ or other changes in the cost of basic inputs, similar goods, or changes in the quantity of goods actually delivered under the contract. Under such a contract of several years duration: 288/

> A series of payments by the retailers would be called for. A series of deliveries of products by the manufacturer would be called for. There would be long and intricate provisions about who has the obligation for warehousing, who is going to advance the stock of capital necessary to get this whole project underway. And what would be the price per unit of goods under a contract such as that, exactly? No one can say! The contract simply never addresses itself to the per unit cost. Ex post, of course, you can take the total payments and divide them by the total number of units received, and come up with a price. But it is not a price that was ever contemplated by anyone.

287/ See Laing, Spurred by Inflation, More Contracts in U.S. Hinge on Price Indexes, WALL ST. J., March 10, 1976, at 1, col. 6.

288/ Testimony of William F. Baxter, DCRG Hearings, Tr. 49-50.

Needless to say, a comparison for Robinson-Patman purposes between sales to a larger retailer under a long-term supply contract and sales to smaller retailers and wholesalers on what is more or less a spot basis, becomes very difficult if not meaningless. Some cases hold that deliveries of goods under a long-term supply contract are not to be considered sales contemporaneous with purchases of goods in spot market transactions. 289/ To the extent that such is the case, the type of marketplace which is necessary for meaningful Robinson-Patman enforcement becomes further removed from the reality of today's business environment.

6. The Assumption That Predatory Pricing Is A Prevalent Practice of Incipient Monopolists

Another major assumption underlying the Robinson-Patman Act's primary line provisions is that "predatory pricing" is a relatively common way in which incipient monopolists try to gain a dominant position in the market place. This idea has persisted well beyond the end of the Depression into our present inflationary period. In 1970, for example, one judge remarked "price cutting, after all, is a time-honored tool of the aspiring monopolist." 290 Recent empirical studies, however, have shown that genuine predation, i.e., pricing below short-run marginal costs, is rare. Moreover, such predation which can actually threaten competition and consumer well-being does not require the

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289/ See Texas Gulf Sulfur Co. v. J. R. Simplot Co., 418 F.2d 793 (9th Cir. 1969).

290/ National Air Carriers Ass'n v. CAB., 436 F.2d 185, 194 (D.C. Cir. 1970).

Robinson-Patman Act for prevention since it can be reached independently under the Sherman Act.

One witness before the Reveiw Group hearing, Professor Kenneth G. Elzinga, summed up the situation: 291/

> There is an expression: those who do not learn from history are condemned to repeat it. It is also true, I am convinced, that those who remember their history can be difficult to disabuse if their history is wrong. The phenomenon of predatory pricing illustrates my point . . . .
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> Under predatory pricing, a large firm, selling in many markets, ruthlessly lowers prices in one of them, driving out all of its rivals there and survives on profits made elsewhere. When its local rivals have met their demise in the targeted market, the company recoups its losses (and more so) by jacking up prices in the depopulated market to monopolistic levels. It is a marvelous story: dramatic, easily told and believable. I can not blame virtually every author of American history textbooks for including such a tale in his or her book, usually through the example of John D. Rockefeller and the Standard Oil Trust. There are only two difficulties with this colorful scenario. One, John D. Rockerfeller didn't use predatory pricing to carve out his monopoly position; and second, for that matter neither has hardly anyone else.

This conclusion was based on empirical studies by several researchers of the actual court records and evidence in a large number of antitrust cases in which the defendants were found guilty of monopolization, and in which predatory pricing practices had been alleged. 292/ In those few cases where

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291/ Statement of Kenneth G. Elzinga, at 1-2, DCRG Hearings (fn. omitted).

292/ McGee, Predatory Price Cutting: The Standard Oil (N.J.) Case, 1 J. LAW AND ECON. 137 (1958); Elzinga, Predatory Pricing; The Case of the Gunpowder Trust, 13 J. LAW AND ECON. 223 (1970); Koller, The Myth of Predatory Pricing; an Empirical Study, ANTITRUST LAW & ECON. REVIEW 105 (Summer 1971) (26 cases).

research showed that the alleged "predation" involved pricing below fully allocated costs, further analysis found that the "predation" which did occur did not harm competition in any meaningful sense. 293/

The reason why genuinely predatory pricing, that is, pricing for an extended period below the incremental cost of producing the good, 294/ is relatively rare is that such a process is expensive and risky for the predator. It is expensive because if a firm wishes to engage in below-cost pricing tactics, the effort must be subsidized either through the revenue from higher prices being charged in relatively non-competitive markets or from other financial resources of the predator.

Additionally, money itself is not free and by using firm financial resources to pay for a predatory pricing campaign, the firm will be foregoing the opportunity to invest money in profitable activities in other areas of the economy. The prophets of predation generally overlook these elements. But the fact is that in order for the firm to gain financial benefit in a predatory pricing campaign, it must reasonably expect that all of its financial losses will be outweighed by subsequent increases in the price and profit level. But this is not usually a realistic expectation: first, because a successful campaign will be highly visible and therefore likely to result in a Sherman Act prosecution and possible conviction under a felony statute; and second because monopoly profits will not materialize unless the

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293/ Testimony of William K. Jones, DCRG Hearings, Tr. 25; Koller, supra note 292, at 108.

294/ See Statement of Kenneth Elzinga at 6, DCRG Hearings; Areeda & Turner, Predatory Pricing and Related Actions Under Section 2 of the Sherman Act, 88 HARV. L. REV. 697, 701-03 (1975); International Air Industries, Inc. v. American Excelsior Co., 517 F.2d 714 (5th Cir. 1975), cert. denied., 44 U.S.L.W. 3488 (1976).

firm can be guaranteed that no new entry will occur thereafter. An assurance of higher prices in the long run is unlikely since the inflated price necessary to recoup the price-war losses will attract new entrants able to produce the product profitably at lower prices. Even rivals driven out of business may reappear when prices become more attractive. It should be noted that two researchers have found that in the Standard Oil and du Pont monopoly cases, which were prosecuted prior to the passage of the Clayton antimerger law, individuals who were forced to sell out to these companies voluntarily reentered the industry and sold out again -- hardly evidence that these businessmen had been frightened into permanent submission. 295/ This is not to say that predatory behavior does not happen -- it may occur when a predator fails to realize the potential loss from such an activity, or because the predator undertakes such a venture for personal, not profit making, reasons. Rather economic logic, coupled with empirical research, indicates that predation is not likely to be a frequent occurrence.

Similarly, supporters of Robinson-Patman oversimplified when they equated predation with price discrimination. One witness before the Review Group identified at least four economic conditions which must be present in order for price discrimination to be tantamount to predation. 296/ First, as just discussed, the price must actually be below marginal cost; if the discriminatory low prices are profitable then the alleged predator does not require higher prices elsewhere in order to subsidize the lower prices. Second, the customers paying the low price

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295/ See Statement of Kenneth Elzinga at 7, DCRG Hearings.

296/ Prepared Statement of William K. Jones at 305, DCRG Hearings.

must in some manner be separated from those paying the high price. If the predator and its rivals all have access to the same customers throughout the country, then the alleged predator and its rivals will compete for the same customers and the predator will not suffer any less harm than its rivals. Third, for the same reason the predator must have more extensive access to customers than its rivals, and particularly to additional customers who can be forced to pay a higher price. Fourth, the low price sales must force at least some of the predator's rivals to curtail their operations or otherwise abandon the market. Unless this occurs, of course, the predator will simply be wasting his money since there will be no benefit from the campaign. In this regard, it should be noted that unless a predator is more efficient than its rivals, it will have to lose relatively more on each sale than its rivals in order to drop the price below the competitors' costs. Consequently, the relationship between price discrimination and actual predation is fortuitous. 297/

Hence, while it is possible that truly predatory discrimination may occur from time to time, both economic logic and empirical evidence demonstrate that the practice has not been and is not likely to be a significant source of anticompetitive behavior. Contrary to the belief of those who enacted Robinson-Patman and the original antidiscrimination provisions of Clayton Section 2, there is little need for a specific statute directed toward this type of discrimination as a supplement to the antimonopolization provisions of the Sherman Act.

297/ It is also worth nothing that companies which produce many products would not need to engage in price discrimination in order to engage in predatory pricing. A large conglomerate corporation, for example, could use profits generated in other products to finance a predatory price campaign in different markets.

7. Conclusion

Resting on the above series of faulty economic assumptions, the Act is made inherently capable of serious harm to society; indeed, the more the statute is enforced and the more it is complied with, the greater becomes its harmful effects on competition. The irony is that Robinson-Patman proves to be quite ineffectual in achieving its nominal goals. The next section of this chapter will describe why the Act is unable to "protect" small businesses and has not done so, and will discuss the reasons why Robinson-Patman is not a useful tool for achieving antitrust objectives.

B. The Inability of the Robinson-Patman Act to Achieve its Goals

Proponents of Robinson-Patman do not rely on any substantive evidence demonstrating direct benefits to the consuming public from the operation of the Robinson-Patman Act. Rather, supporters have largely accepted at face value the personal perceptions of those who daily experience the risks of the marketplace, and of those who have been disadvantaged in business by lack of bargaining power. Such observations tend to focus on the success or hardship of particular firms rather than on the condition of competition generally.

Those in favor of the Act have stated several reasons why they believe retention of the Act would be in the public interest. First, they claim that Robinson-Patman offers protection and assistance to small businesses, that the law does so in a manner that is in accord with the antitrust laws, and that it does not impose additional "regulation" on the private sector. Secondly, they allege that Robinson-Patman provides a needed supplement to the other antitrust statutes by preventing predatory activities which cannot be reached under these laws. Lastly, they suggest that the Act can significantly reduce the trend toward increased concentration in the economy. It is argued, therefore, that any consumer benefit from an initial lowering of prices which may result from the removal of Robinson-Patman would be outweighed in the long run by less competitive markets and higher prices.

These claimed benefits of Robinson-Patman, if supported by pursuasive evidence, would be worthy of public support. The Report will, therefore, turn to an evaluation of the objectives which supporters of Robinson-Patman have stated the Act is intended to achieve.

1. Robinson-Patman is an Effort to Interfere with Normal Evolutionary Cycles in Distribution

Distribution, the business arrangements by which goods get from their producers and manufacturers to the consumer, is a vital sector of our economy. Traditionally, the distribution of consumer goods has been thought of as a three-tiered process, involving the manufacturer of the product, the retailer who sells the product to the consumer, and the wholesaler who acts as the intermediary between the manufacturer and the retailer. The American consumer has a vital financial interest in the efficiency and effectiveness of these channels of distribution: according to government statistics, of the $283 billion paid by the consuming public in 1967 for purchases of durable and non-durable commodities (at 1967 prices) thirty-four percent, or over $100 billion, went to pay wholesalers and retailers for their services. 298/

Yet, for all its size, surprisingly little attention has been paid in the debate on Robinson-Patman to the fact that distribution is indeed an "industry" and that "innovation" and technological change in the distribution industry were significant parts of the maturation of the American economy over the last century. These changes were as significant as the replacement of the handcrafted product by the assembly line or the replacement of the multi-story urban factory by the single story suburban plant. The public, however, does not regard changes in the method of retailing as having the same importance as the sale of a new "product" to them, for example, the introduction into the retail market of color television, or television itself for that matter.

Because of this failure to perceive change in the distribution sector as innovation, and hence valuable, the Robinson-Patman debate centers exclusively on the issue of whether it is appropriate to protect small businessmen from "large corporation" organizations; no consideration

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298/ The Input-Output Structure of the U.S. Economy: 1967, SURVEY OF CURRENT BUSINESS, February 1974, at 32. In 1975, consumer spending on durable and non-durable goods reached $538 billion. National Income Accounts of the U.S., 1929-1975, SURVEY OF CURRENT BUSINESS, January 1976, at 39.

is given to whether such protection would, if successful, serve to inhibit innovation in distribution, or to impede development of more efficient forms of business organization, or to forestall the establishment of new types of retail outlets. Nor is consideration given to the consumers who might benefit from and desire such changes.

During the 1920s and 1930s when much of the debate on protecting small businessmen from chains took place, refrigerators began to replace ice boxes as the normal means of household refrigeration. Of course, everyone perceived the refrigerator as a much desired innovation in keeping consumer perishables cold, and most members of the public and their representatives in government undoubtedly viewed the introduction of the refrigerator as a net gain to society. On the other hand, the introduction of the refrigerator had an extremely adverse effect on one segment of the economy -- those who were in the business of providing ice. Many of these ice companies which were forced out of business by the refrigerator were undoubtedly small local businesses, and the refrigerator manufacturers who in effect replaced them were much larger and generally operated on a nationwide basis. Today, most people would dismiss out of hand the argument that the introduction of refrigerators should have been restricted in order to protect those small businessmen and in order to keep as high as possible the number of small businessmen in the American economy. Likewise, few people would have suggested that the introduction of the automobile be abandoned simply to protect the blacksmiths, carriage manufacturers, horse dealers, veterinarians, harness makers, and others who were affected by the coming of the automobile. Such change is (or has been until recently) viewed as a positive benefit to society. Because of its immediateness and visibility, such change was evaluated on its own terms and not in terms of the battle between incumbent businessmen and the entrepreneurs who would replace them if their innovation were to become part of the accepted pattern of economic life.

In the case of distribution, however, few people are even conscious of the changes in the relative functioning of business intermediaries, e.g., wholesalers with whom the public does not deal. Yet these invisible changes -- consolidation of small independent warehousing operations into one central warehouse, the integration of the warehousing function into the retailing function or the absorption of the warehousing function by manufacturers -- can act to decrease the cost of interbusiness transactions and increase the ability of manufacturing organizations to be more responsive to the needs of retailers whose sales to the public ultimately determine the demand for the manufactured product.

On the retailing level, there have been many similar innovations: the introduction of the department store in the last century; the introduction of the supermarket in the 1930s; the more recent introduction of the combined food and consumer goods "superstores," fast food outlets, home furnishings "warehouses," and the development of "life style" oriented shops, such as those selling blue jeans. At the same time, the location of primary retail activity has shifted from downtown shopping areas, first to suburban "strip" shopping centers and then to the more recent enclosed suburban shopping "mall." Here too, businessmen who could not respond to these changing ways of retailing were put under severe pressure staying in business, while those who were in the forefront of, or could readily adapt to, such changes were relatively better off. While consumers were ready to accept such changes in the nature of the retail outlets from which they did business, arguments could still be made -- witness the debates on fair trade legislation -- that new forms of retailers, such as the "discount houses," should be hindered so as to preserve the business status quo.

The distribution of consumer goods has been one of the more dynamic sectors of the American economy. On the retail level merchants adapt to new products, new consumer lifestyles, and different demographics of population, age, and location. They must also cope with changes in the relative importance of price, service, and product quality to the varying income classes of the buying public, and with new concepts in merchandising like the emergence of mass marketing and "nonstore" retailing such as catalogue sales firms. 299/ In wholesaling there is continual change arising from the emergence of new products, relative variation between the types of merchandise sold by the manufacturers and retailers in a given industry, changes in technical efficiencies of warehousing, and in the relative efficiencies among warehousing operations owned by manufacturers, retailers, or retailer's cooperatives. 300/ In this

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299/ See Davidson, Changes in Distribution Institutions, in E. KELLY & W. LAZER, (ed.), MANAGERIAL MARKETING, 420, 423-25 (1973). See also Davidson, Bates & Bass, The Retail Life Cycle, HARVARD BUS. REV. Nov.-Dec. 1976 at 89.

300/ See McKeon, Conflicting Patterns of Structural Change in Wholesaling, in BOONE (ed.) MARKETING CHANNELS 95, 112-113 (1973).

changing environment, of course, individual businessmen must also meet the continuing competition from competitors who, while doing business in approximately the same manner, may do it more efficiently, or may simply be better able to satisfy the changing demands of their customers.

This constant change gives rise to a "life cycle" by which the various modes of distribution move from their inception as an innovative way of doing business, through a period of maturation in which they become successful -- if they are indeed more favored by purchasers than the way of doing business which they are designed to replace -- to a later period in which they are in turn eclipsed by new business methods. Students of the distribution process have put forward several theories to explain the dynamic changes which have occurred in the various channels of distribution. Under the so-called "wheel of retailing" hypothesis: 301/

> [N]ew types of retailers enter the market as low status and low margin institutions. These institutions are located in less convenient locations thereby saving on rentals, offer few services and are inexpensively furnished. Gradually as these institutions mature they develop into institutions offering many services, acquire more elaborate facilities, feature higher prices and carry merchandise lines that convey higher status. Discount houses and supermarkets are examples of these kinds of institutions. Automatic merchandising [vending machines], the growth of branch department stores and the rise of suburban shopping centers are exceptions to the wheel hypothesis. (Footnote omitted.)

301/ R. MICHMAN, MARKETING CHANNELS, 45 (1974).

Another theory is the so-called full-cycle theory: 302/

> [T]he distributive institution enters as a low margin, low price entrepreneur, gradually increases its margins, and at a certain point gradually begins to decrease its margins. External and internal environmental circumstances determine when the point is reached for margins to gradually decrease from previous high margins. Services are diminished by the institution but locations are expensive to change and usually remain the same. Another form of this theory is that the institution may either construct or acquire another organization that will assume the role of a low margin institution.

Other theories examine the competitive reaction of firms to new entrants into distribution, and also focus on the process of "natural selection" by which those institutions that remain are the ones best able to fulfill the changing requirements of the buying public.

Regardless of which of these theories most accurately describes the process of change in distributive institutions, the important lesson to be learned from observation of the events of the past half century is that much change has indeed taken place, a "retailing revolution" according to some. The process has been, and in our system inherently is, one of "creative destruction." 303/ That is, "channels of distribution undergo continuous and occasionally dramatic change as economic agents search for new and better ways to perform the marketing functions." 304/ In this process, those who do not innovate, or who no longer serve the needs of the purchasing public, fall by the wayside, while those with new and better ideas, or who are ready to

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302/ Id. at 47.

303/ P. KOTLER, MARKETING MANAGEMENT 66 (1972).

304/ Id. at 558.

adapt to a changing economic environment succeed. 305/ Some of these (such as W.T. Grant) may be large enterprises, others may be small.

Not only do changes in distributive institutions lead to a variance in the "mix" of business organizations serving the marketplace, but the process also leads to changes in the power relationships among the various tiers of the distribution system, the manufacturers, wholesalers, and retailers. Before the Civil War, wholesalers were the "channel captains," the ones in the distribution channel who made the major decisions about the price and type of goods to be sold. From the Civil War until about World War II, manufacturers were the leaders, deciding what products would be produced and how they would be sold. Since then, many major retailers have taken over the leadership role in some industries and through their buying power, and concomitant use of private brands and specifications, have a major impact on the type of goods which are produced for consumers and on the ways in which they will be sold. 306/

Because innovation potentially threatens the existence of the various firms in an existing channel of distribution, or at least, threatens to cause them to change the way in which they do business, those who fear a new way of doing business will respond both economically and politically. Eventually, though, the form of doing business that makes the most economic sense and which has the greatest appeal to the consuming public will win out and competitors will either adjust to the new way of business or leave the

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305/ See Testimony of Louis Fox at note 341, infra.

306/ MICHMAN, supra note 301, at 48, 193.

marketplace: 307/

> When new institutions first appear, the typical pattern is one of institutional conflict followed later by accommodation. The established institutions band together and use all their power to thwart the new institution. One thing they do is threaten to break off business relations with those who supply the new institution. This was the position in which national-brand appliance manufacturers found themselves when they started dealing with discount houses, milk producers when they allowed their brands to appear in vending machines, and drug manufacturers when they started to sell some of their products through food outlets. Another weapon of the established retailers is to lobby for restrictive legislation against the new retailing outlets. They try to pass laws placing special taxes on these organizations, or restricting their hours of operation, or preventing them from selling certain goods. These tactics, plus a great amount of scare propaganda, are used by vested retailing interests to destroy or slow down the growth of newer retailing firms.
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> But the newer firms, where they represent a real advantage, generally survive this onslaught, and in the next phase the more progressive established firms begin to accommodate their selling methods to the new ones. They reduce their margins, cut down some of their frills, form chains, expand their parking space, and in general, reduce the competitive advantage of the newer firms. In time the differences between them grow very blurred.

Seen in this context, Robinson-Patman may be perceived as part of a political response by small independent merchants and independent wholesalers to the increased growth of a new type of retailing organization, the chain store. As previously discussed in Chapter III(C), support for Robinson-Patman was particularly strong from the wholesaling community which, correctly, saw the coming of chain stores and their vertically

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307/ KOTLER, supra note 303, at 67.

integrated wholesaling-retailing operations as a threat to their survival. Similarly, the independent retailer feared the ability of multi-store firms to bargain more successfully with suppliers and feared their ability to pool the operating profits and losses of several stores in several geographic areas. Thus, occurring simultaneously were a revolution in distribution and a great depression. The former was a positive force, the latter a negative one. But each joined in the creation of a common effect: the destruction of the small businessman's sense of present and long-term security and the universal perception of the loss of fundamental American values.

In the area of food retailing, the coming of the supermarket in the early 1930s added to the fear of the small grocer, because it implied the coming of physically-different food stores which were often more attractive to the consumer and with which existing retailers in their smaller stores could not compete. In response to these honest fears, the Robinson-Patman Act and other legislation was enacted 308/ to reduce the natural competitive advantages of chain stores. As introduced, Robinson-Patman was designed to neutralize two advantages of the chain store. First, its section on

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308/ For a more complete discussion of legislative responses to the development of chain stores, see chapter III(B), *supra*, p. 108.

on customer classification (later to be dropped in the legislative process) and its prohibition on payments in lieu of brokerage, both taken from NRA Codes of Fair Competition, were designed to inhibit vertical integration by retailers into the wholesaling function, thus preserving the existing classes of middlemen. Second, the general prohibitions of discrimination which would adversely affect the status of a "competitor" were designed to forbid larger buyers from using their superior bargaining power to reduce manufacturers' prices to them.

2. In Spite of Its Protectionist Purpose, Robinson-Patman Cannot in The Long Run Significantly Affect The Success or Failure of Small Businesses as a Group

One of the more startling discoveries about Robinson-Patman is that for all its regulatory interference with short-run pricing it really does not appear to be helping small business; the growth of larger firms in the retailing trade has not been significantly retarded. In the grocery business, for example, the percentage of sales represented by chains of four or more stores has grown from 36.7 percent in 1939 to 51.9 percent in 1963 to 62.7 percent in 1972. For chains of 11 or more stores, the percentages of sales was 34.4 percent in 1948, 47.0 percent in 1963, and 57.0 percent in 1972. 309/ The fundamental reason for this lack of success cannot be attributed to ineffective Robinson-Patman enforcement, since this period of growth of multi-unit retailing establishments included the era of greatest Robinson-Patman Act enforcement by the Federal Trade Commission. Moreover, the continuous threat of private treble damage actions under Robinson-Patman, particularly in food industries, may inspire more pricing caution in sellers than possible government enforcement. The basic problem with Robinson-Patman is that it does not and cannot deal with the numerous other factors, some more important than discrimination in the cost of goods purchased, which determine the success or failure of particular businesses. And it is, of course, the process of exit and entry by individual businesses which cumulate into the share of the business done by independent retailers and by multi-unit establishments as a class.

309/ 1966 FTC FOOD STUDY, note 105 , *supra*, Table 9 at 300; 1972 CENSUS OF RETAIL TRADE, SUBJECT SERIES, ESTABLISHMENT AND FIRM SIZE (RC-72-S-1), Table 2a (1975).

Thus, in order to answer the question whether Robinson-Patman can actually "protect" the individual small businessman--and it is the individual, small business Congress has really desired to protect--one must evaluate the actual likelihood that a law dealing with one factor affecting competition can really have much impact on the long-run success or survival rates of small businessmen as a class.

a. Responsiveness to Consumer Preference, Not Economic Power, Ultimately Determines the Success or Failure of Competing Distribution Systems

Retailing, as previously discussed, is a dynamic sector of the economy. As business institutions evolve, as consumer buying habits change, and as the economy as a whole experiences its ups and downs, businessmen are continually placed under pressure; some survive and some do not, often with little regard to differences in the cost of goods purchased. In order to evaluate the ability of Robinson-Patman, or any other price discriminations statute to serve the Congressionally enunciated policy of preserving and enhancing small business, the policy maker must first take a realistic look at the American distribution system. For if there is no significant public benefit which may be achieved in the pursuit of this goal, it cannot be used to balance the substantial cost of Robinson-Patman.

A realistic view of retailing shows that its entire structure is changing from the model of independent manufacturers, wholesalers, and retailers which characterized the distribution sector in the early 1930s. For example, "vertical marketing systems" have emerged as the dominant organizations for selling goods: 310/

310/ Davidson, supra, note 299, at 421-22.

> Conventional marketing systems are being rapidly displaced by vertically organized marketing systems as the dominant distribution mechanism in the economy. Conventional channels are those fragmented networks in which loosely aligned and relatively autonomous manufacturers, wholesalers, and retailers have customarily bargained aggressively with each other, established trade relationships on an individual transaction basis, severed business relationships arbitrarily with impunity, and otherwise behaved independently.
>
> Vertical marketing systems, by way of contrast, consist of networks of horizontally coordinated and vertically aligned establishments which are managed as a system. Establishments at each level operate at an optimum scale so that marketing functions within the system are performed at the most advantageous level.

Analysts have described three types of businesses as suitable for operation as vertical marketing systems. 311/ The first, corporate systems, are generally out-growths of chain store organizations. They become vertical marketing systems when they take over not only their own wholesaling and internal distribution functions, but also certain manufacturing functions as well. Similarly, some manufacturers in the clothing, paint, and tire industries also own retail outlets. According to one source, Sears, Roebuck obtains 50 percent of its merchandise from manufacturing facilities in which it has an equity interest; many supermarket chains obtain 15 percent to 20 percent of their merchandise from their own manufacturing plants. 312/ Major chain organizations, those having 11 or more units, and the greatest

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311/ See Davidson, supra note 299, at 422-23, KOTLER, supra note 303, at 558-60.

312/ McCammon, Perspectives for Distribution Programming, in VERTICAL MARKETING SYSTEMS 45 (L. BUCKLIN ed. 1970), quoted in KOTLER, supra note 303 at 559-60.

potential for becoming vertical marketing systems, were responsible for almost 32 percent of all retail sales in early 1975, as compared to 19 percent in 1948. 313/

The second type of vertical marketing system is the contractual system. It includes: wholesaler-sponsored voluntary chains (prevalent in the food and drug industries); retailer cooperatives which undertake the wholesaling function (these may or may not sponsor private brand names or advertising for members of thecooperative); and franchise organizations. The last of these may be manufacturer-sponsored retailer franchises, manufacturer-sponsored wholesaler franchises or service firm-sponsored retailer franchises, such as fast food restaurants. The development of contractual marketing systems is perhaps the most important development in the retailing market in terms of evaluating the need for Robinson-Patman, because such contractual systems permit their member businessmen, often small firms, to achieve marketing power, a group identity and a consequent ability to compete more effectively with large enterprises. A 1970 study suggests "that 35 to 40% of all retail trade is accounted for by some form of voluntary chain, cooperative, or franchising organization." 314/ Indeed, in the food industry, the percentage of independent retailers affiliated with some wholesaler group or cooperative has expanded from 46 percent to 83 percent during the period from 1947 to 1964. 315/

313/ 1975 STATISTICAL ABSTRACT OF THE UNITED STATES, 773; U.S. CENSUS OF BUSINESS, 1948 VOL. I, at 3.02-.04.

314/ Davidson, supra note 299, at 422.

315/ 1966 FTC FOOD STUDY, supra note 105 , at 41.

In the third type of vertical marketing system, the administered system, sellers develop comprehensive programs for the marketing of a particular product or line of products in retail outlets. There are apparently no statistics on the magnitude of this type of relationship, which may be found in food products, certain clothing, and in the home appliance industries.

Concurrent with the growth of the so-called vertical marketing system has been the increasing specialization of retailers as either mass merchandisers or speciality shops selling a single product: 316/

> Retail trade is becoming increasingly polarized at two extremes. On the one hand are mass-merchandising operations that have successfully implemented supermarket approaches. This group includes the general merchandise types of discount or promotional department stores, and also the more specialized establishments with a large mass appeal. . . . At the other pole are highly specialized boutique types of stores which carry a deep assortment of a very specialized line, often limited to a concept or a "look", as opposed to commodity types. . . . Such shops tend to be strong on services and are often distinguished by the provision of consumption advice as opposed to conventional selling approaches.
>
> At both poles, establishments tend to be organized into vertical marketing systems upon the achievement of scale. Between the poles are conventional and often non-programmed single-line stores of the family apparel, hardware, drug, and jewelry types. For these stores and their supply systems, the polarization is suggestive of increased obsolescence and profit difficulties in the 1970s.

Thus, according to another observer, "In general, the new competition in retailing is no longer between independents but rather between whole systems of centrally programmed networks (corporate, administrative, and contractual) competing against each other to achieve the best economies and customer response." 317/

316/ Davidson, *supra* note 299, at 423-24.

317/ KOTLER, *supra* note 303, at 562.

To the extent that this trend continues the small business retailer, in order to be successful, will have to provide a different type of merchandise, shopping convenience, or service-price mix than either the large business, or the affiliated independent businessmen. To a large degree, this transition has already taken place. Therefore, Robinson-Patman's assumed struggle between the great and the small retailer is at odds with reality: 318/

> [Robinson-Patman assumes] that small retailers are in head to head competition with large retailers. And that really isn't true. They perform quite a different function in the economy. They have higher costs, does that mean they are less efficient? No. Because in order to talk about the costs of the distribution function, you have to take the ultimate consumers' shopping costs into account. And the function of the small retailers is to reach out there toward the customer, and reduce his shopping cost by putting a small establishment near him. And that reduces the sum of the customer's cost, plus the retailer's costs. The function of the large retailer is to provide a big establishment, not terribly conveniently located, and the same people will go to one at one time, and the other, another time, depending on the nature of the shopping function they are performing.
>
> So what happens if prices to small retailers are, if the differential between their costs and the big retailers' costs are augmented by half a percent? The smaller retailers will not disappear en masse. That might occur if they really did perform the same function as the big retailers and were competing head to head. What occurs, instead, is a modest reduction in the dispersion of small shops out toward the customer, very slightly increasing his direct shopping costs to achieve a new equilibrium with the lower prices. The result is a very modest and less dramatic proposition than massive disappearance of small retailers. You get very gradual change in balance between large and small retailers. But the critical feature of it is small retailers are performing different functions in the society, and it isn't as if everyone was standing on a knife edge, a half a cent would tip you one way or the other. That is a misconception.

318/ Testimony of William F. Baxter, DCRG Hearings, Tr. 55-56.

Hence, the so-called convenience food store is able to compete at unabashedly higher prices, sometimes immediately adjacent to a large supermarket, because it offers the convenience of a small selection of frequently purchased goods, coupled with longer hours and quick check-out time. As an example of this, one of the witnesses before the Review Group recorded that in purchasing a carton of cigarettes at a chain convenience store, he was informed that a carton would be cheaper at some other establishment since the convenience store only sold cigarettes at the per-pack price. 319/ In that case, the convenience store was really catering to those persons who wanted to buy a single pack of cigarettes in a hurry and were willing to pay for the privilege.

Similarly, the customer is often also willing to pay for a special ambience where he shops. For example, certain tobacco shops which cater to those who like to feel that they are "sophisticated" smokers may be quite successful in competing for the trade of not only those who wish to buy specialized tobaccos, but also those who wish to purchase tobacco products otherwise available from a large drugstore.

Failure of businessmen in the channel of distribution, both wholesalers and retailers, to adapt to changing market conditions will attract to the marketplace new businesses more responsive to the wishes of manufacturers or retail customers. One study of changing patterns in wholesale institutions identified several wholesale industries where the merchant wholesalers increased their share of the wholesaling function at the expense of sales branches operated by

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319/ Testimony of James D. McKevitt, DCRG Hearings, Tr. at 383-84.

manufacturers: 320/

> Briefly, the thread that links the merchant wholesalers of the above twelve trades appears to be their willingness to adjust to a changing environment. The merchant wholesalers in these twelve trades have not been passive "ordertakers." They have become more sensitive to the needs of their customers and their trade channel system. They have recognized opportunities; even more important, they have taken the necessary steps to capitalize on these opportunities.

The study also identified certain wholesaler areas where manufacturers' sales branches gained at the expense of the independent wholesaler. Interestingly, one of the sectors singled out for poor performance were the drug wholesalers, one of the proponents of Robinson-Patman in the 1930s. 321/ The study summarized the situation thusly: 322/

> The drug and hardware trade channels are examples of traditional merchant wholesaler and retailer rigidity in accepting and adjusting to environmental change. The primary changes were the development of a large number of new products, the advent of scrambled merchandising [*i.e.* - the selling of several product lines in one store, such as a drugstore], and the growth of large-scale retailers. The drug channel was affected by all the above developments and the hardware channel was affected primarily by the latter two developments at the retail level. The manufacturers' reaction in both channels to the wholesalers' failure to adjust was identical -- the establishment of branches. To the credit of the wholesalers, they began to do something about their plight, although only after the sales branches had gained a substantial share of wholesale sales. In both channels, the initial reaction was specialization by product line. Some traditional general-line wholesalers shifted to a specialty-line operation but it is believed that most of the "shift" from general-line to specialty-line wholesalers is the result of the establishment of new specialty-line wholesalers. Also, some general-line wholesalers dropped

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320/ McKeon, *supra* note 300, at 104.

321/ See text at note 220, *supra*.

322/ McKeon, *supra* note 300, at 104-05.

some traditional services performed for their retail customers and added the others. The added services were in the area of retail location analysis, forecasting, financing, and store layout. The wholesalers' latest strategies in the drug and hardware channels have been establishment of wholesaler-sponsored and retailer-sponsored cooperatives.

The most important observation to be made in this discussion of changing environment of businesses is that no statute can stop -- nor should it attempt to stop -- the functioning of consumer preference. Whenever a business runs into difficulty because it is losing sales to a competitor, the reason for the seller's loss is usually the customer's perceived gain. When given a choice between two competing ways of doing business, customers will "vote" with their purchases as to which price/product/service mix they prefer. Thus, "part of the cost savings of supermarkets was the result of the consumer's willingness to assemble her own order, arrange for credit elsewhere, and deliver her own orders to her home" 323/ in return for a lower price. This trade off between price and service permits people to make choices based on their own incomes and preferences, a fact which was noted in the 1935 final report of the Federal Trade Commission on chain stores: 324/

> [I]n the smaller towns, at least, people of lower means patronize the chain stores to a greater extent than do those with larger incomes. Those who state that they purchase more than half from chains amount to 17 percent of the persons with larger means replying to the Commission's inquiry, 22 percent of the medium-income group, and 35 percent of those with smaller means. The most frequently stated reason for patronizing chain stores is lower prices, and no other one reason for buying from

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323/ Id. at 112.

324/ 1935 FTC CHAIN STORE STUDY, at 66-67.

chains approaches it in importance. The reason most often advanced for buying from independents is credit, followed by delivery service, and by loyalty to local enterprise.

One of the witnesses testifying for the Review Group, William Woods, Washington representative of the National Association of Retail Druggists, seemed to acknowledge that consumer choice did play a part in the growing market share of larger chain drugstores versus that represented by small independents: 325/

> Mr. Flexner: Mr. Woods, might not one reason for this decline in market share that apparently is currently evidenced and has been happening over time be simply the result of the consumers' choice?
>
> Mr. Woods: Well, it could be, but you can argue that both ways. We know of consumers complaining about the thing I just read, but, perhaps a factor in some places, and consumers are not all alike.
>
> If a consumer wants to drive many miles or have some inconveniences to save a few cents, that is his business, but I do not think that the person who would like to have convenience of a pharmacy near him, such as an older person who does not want to go that far and is willing to pay more for service, I think he should have that opportunity.

The hard fact is that presented with the choice between low service and inconvenience at a low price and high service and convenience at a higher price, relatively more people may opt for the low price -- especially poor people. If those who complain about low service and inconvenience form a sufficient number of persons to support a retail establishment catering to their needs, that establishment will survive. If those people wanting the higher service and the higher price do not form a sufficiently large population to make such an

325/ DCRG Hearings, Tr. 445.

establishment viable, such an establishment simply will not survive in that form without at least some indirect subsidy from those consumers who would prefer a lower price, poorer service option. No amount of legislation designed to prevent price discrimination can reverse the trend.

Most of the factors, then, leading to the success or failure of a small businessman are outside the control of Robinson-Patman. According to a Dun and Bradstreet report on business failures, "regardless of a recession or a boom, inexperienced or inept management is the underlying factor in nine out of every ten failures. But the problems which prove insurmountable to the untried or incompetent businessmen change with the economic climate." 326/ In retailing particularly, it is the first few years of a business operation, when experience is the least, in which most failures are likely to occur. Of the 4,234 retail failures which occurred in 1974, 40.5 percent involved businesses in existence three years or less, 66.2 percent involved those in existence five years or less, and only 15.4 percent involved businesses of more than 10 years' experience. 327/

326/ DUN & BRADSTREET, THE BUSINESS FAILURE RECORD, 1974, at 3 (1975).

327/ *Id*. at 10.

b. Large Scale Businesses Have Other Advantages Over Small Businesses Because Of Flexibility And Efficiency Which Are Beyond The Reach of Robinson-Patman

Large firms have many competitive advantages with which Robinson-Patman cannot deal. The Act's restriction to commodities of "like grade and quality " can be avoided by large purchasers, as explained by the Director of the Bureau of Economics at the Federal Trade Commission: 328/

> [G]iant business corporations enjoy more strategic options than their smaller rivals. If you tell a firm like A&P or Dart Industries that its suppliers cannot pay it a brokerage allowance,it can adapt in a variety of ways -- e.g., by integrating vertically and producing its own requirements, or by dealing only with suppliers who serve it exclusively, or by ordering private-label items differentiated from the merchandise its suppliers sell other retailers. Much smaller retailers lack such flexibility, and the tactics they must adopt to hold their own against the A&Ps and Safeways and Rexalls often bring them into conflict with Robinson-Patman while the giants go unscathed.

More importantly, large firms often have long run advantages which do not involve price per cost of goods sold, and are hence beyond the reach of the Act. For example, large firms may have lower costs for the entire channel of distribution of which they are a part. Such lower costs may result from more efficient actual operation or from the integration of various wholesaling and retailing functions and consequent elimination of certain costs associated with independent wholesalers. This fact was dramatically demonstrated by the 1935 final report of the FTC's chain study. The report found that only a relatively small portion of the chains' lower price was explained by these lower prices for purchased items, including

328/ Prepared Statement of F. M. Scherer, Subcommittee Hearings, pt. 2 at 145.

all special allowances granted to the chain. The figures for grocery stores, depending on whether the advantage was weighed on the basis of chain store or independent sales volume, range from 16.6 percent to 19.9 percent in Detroit, 19.16 percent to 35.8 percent in Memphis, 20.5 percent to 23.6 percent in Washington, D. C., and 3.01 percent to 4.8 percent in Cincinnati. 329/ In the retail drug trade, the figures as to the percentage of selling price difference explained by purchase price differences, again depending on the weighing factor used, were 9.7 percent to 10.8 percent in Washington, 7.7 percent to 5.4 percent in Cincinnati, 5.3 percent to 3.9 percent in Memphis, and 17.4 percent to 18.3 percent in Detroit. 330/ It is obvious that even with the complete elimination of lower sales prices to chains (and some of these lower prices were cost justified), the remaining 80 percent to 90 percent of the cost difference would have remained and the smaller stores would have continued at a disadvantage if competition were confined solely to price.

A 1939 study by the 20th Century Fund also found that in many areas of retailing, particularly the grocery store trade, chain stores had a lower cost of retailing than did independents. 331/ Just as importantly, that same study concluded that in six out of the seven types of businesses surveyed, including food and drugs, the cost of chain store warehouse

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329/ 1935 FTC CHAIN STORE REPORT 55.

330/ Id. at 56.

331/ TWENTIETH CENTURY FUND, DOES DISTRIBUTION COST TOO MUCH? 134-40 (1939).

operations was significantly lower than the costs of independent wholesale merchants and manufacturers' sales outlets. 332/ Indeed, the 1935 Federal Trade Commission study seemed to point a finger at independent wholesaling as a cause of higher prices to independent retailers: 333/

> The studies of grocery prices contain indications that the difference between chain and independent selling prices is appreciably less on merchandise delivered directly by the manufacturer to retail store units, whether chain or independent, than on goods handled through wholesale or chain-store warehouses. Although the absorption of the wholesale function by the manufacturer does not necessarily reduce the cost of goods to the consumer, it apparently tends to reduce differences between chain and independent prices.

Large firms are also able to secure an advantage over their small rivals through vertical integration and better control of flow and specification of merchandise in accord with the special needs of their customers. These advantages go beyond the mere avoidance of Robinson-Patman; they enable a larger purchaser to manage its own production of merchandise and thereby to ensure its ready availability when needed, or in the case of individual specifications, to tailor-make the merchandise to meet a perceived selling point with the customer. By contrast, the small purchaser must sell whatever it is that the manufacturer decides to produce and must await the manufacturer's decision to change his line. Thus, although an individual retail store may not have to be very large to achieve efficiencies of <u>in-store operation</u>, much larger enterprises may be needed to achieve full efficiencies in distribution and manufacturing. The Federal Trade Commission in its

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332/ Id. at 178-181.

333/ 1935 FTC CHAIN STORE REPORT at 34.

statement on merger guidelines for food distribution industries concluded: 334/

> Economies of retail selling are achieved primarily at the store level and ordinarily can be achieved by units with annual sales of between $1 million and $2 million. Economies of scale in performing the warehousing function most probably do not extend beyond the $75 to $100 million range. Advantages associated with sizes beyond this scale relate primarily to manufacturing operations, private label programs and field buying of perishables, although economies in these areas can be obtained by a company with retail sales of $500 million.

While a $500 million corporation is smaller than the largest firms in the grocery industry, it is not a small business.

Larger businesses also enjoy efficiencies in advertising. Since the cost of newspaper, electronic media, or direct mail advertising varies according to the size or type of advertisement used and the number of persons reached, it is not directly proportional to the volume of business done by the advertiser. Hence, an organization with a relatively larger sales volume can spread its advertising costs over this volume to achieve a smaller per unit cost. A 1966 FTC study summarized the situation in the food industry: 335/

> There appear to be marked advantages of large size in local newspaper advertising. These advantages stem from a combination of real economies of scale, pecuniary advantages of size, and the advertising rate structure of most newspaper advertising. First, and probably most important, real economies of scale occur because a retailer can spread its newspaper advertising over a larger volume of sales. Second, newspapers generally have significant volume discounts that may only be received by retailers which buy substantial advertising linage during the year [not covered by Robinson-Patman since advertising

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334/ Commission Enforcement Policy With Respect to Mergers in The Food Distribution Industry (1967) 1 CCH Antitrust And Trade Reg. Rep. ¶4525 at 6906.

335/ 1966 FTC FOOD STUDY, _supra_ note 105 , at 276-78.

> is a service, not a "commodity"]. Third, a retailer ordinarily receives a larger absolute volume of promotional allowances from its suppliers when it has a large market share than when it has a small one, particularly in local markets. Other things being the same, a retailer with 5 percent or less of a local market may have net advertising costs, per dollar of sales, three or four times as great as the retailer with a 20 percent or more market share. This cost disadvantage could amount to 0.8 cent per dollar of sales or more. (Footnote omitted)

The ability of a multi-unit enterprise to average its profits and losses over all of its units may enable it more effectively to respond to market changes in a particular area, while the smaller establishment may find that the lower profit margin caused by localized pricing promotions or declines in demand will again put it under greater pressure. In this regard, it should be noted that the 1935 Federal Trade Commission study, in discussing the lawfulness of the charging of different prices in different outlets of the same chain, concluded that such practices came within the "meeting competition" defense of the original Section 2 of the Clayton Act, which is quite similar to that contained in the Robinson-Patman Act's revision of Section 2: 336/

> Variation in price between different branches of a chain would seem to be a discrimination, the effect of which 'may be' to produce the forbidden results. It is one thing, however, to reach such a broad conclusion on the results of this practice by chains in general and quite another to prevent by legal means its use by some particular chain. The reason is that the Clayton Act itself specifically permits price discrimination 'in the same or different communities made in good faith to meet competition.' The Commission has no evidence which would establish that price discrimination by chain stores has not been in good faith to meet competition and there is good ground to conclude that in many cases it has been for that purpose.

336/ 1935 FTC CHAIN STORE REPORT 51.

Larger enterprises may also have an advantage over smaller enterprises in that their larger buying organizations give them the ability to find the best price according to market conditions in several areas of the country. Additionally, their larger staffs permit greater specialization and ability to select and test particular merchandise before purchase. The 1935 FTC Chain Store Report gave an example of this circumstance: 337/

> One large grocery chain is usually successful in buying under the list price because of its keen knowledge of the markets. For example, it will frequently play the market of one State against the market of another with threats that if the price at which goods can be obtained from the other State is not met, the manufacturer will not obtain the business. Similar chains and wholesalers, it was reported, who do not feel the pulse of other markets in this way, do not secure the preferential treatment.

Finally, larger, more aggressive organizations may be more adaptable to change and to reworking their entire operation to meet competition. As one study put it: 338/

> Many merchants particularly small ones are not growth minded. These merchants desire the security of selling products that are familiar and close to their self-images. Consequently, these merchants would rather specialize than diversify their product offerings. Specialization affords an expertise. Expansion would bring many problems with which these merchants are not prepared to cope and would require adjustments in the day-to-day operations of their businesses.

A study of the retail drug industry for example, concluded that the industry was under much pressure for change, not only from chain drug stores, but from central drug dispensaries associated with professional buildings or

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337/ *Id.* at 25.

338/ MICHMAN, *supra* note 301, at 53.

health maintenance organizations and from those who criticized its high prices. Despite this pressure for change, the study found resistance to change among druggists: 339/

> Although the druggist hears these statements of dissatisfaction, if he follows his past pattern, he is likely to resist these changes as he has been trained to do in the College of Pharmacy and past practice with legal and association action. The tradition in pharmacy has been to regard price cutting as unethical, unprofessional, and not helpful in solving long-run problems. . . . In one [1955 pharmacists'] text book illustrating pricing methods, all illustrations show markups of 31-50% and historical data are cited to show that this type of markup has been maintained in the drug trade since 1900. (Footnotes omitted)

As an example of the pharmacists' attitude toward price cutting the study cites a 1953 survey of druggist reaction to price competition on prescription drugs. The results showed that 67 percent would try to engage in better salesmanship, 50 percent would offer off-street parking, 62 percent would try to feature complete drug stocks, 40 percent would relocate their store, 33 percent would add a new store front, 30 percent would increase advertising, and only 10 percent would cut prices. 340/

In testimony before the Review Group, Mr. Louis Fox, President of Associated Wholesale Grocers, a large cooperatively owned wholesale food distributor in Kansas City, Kansas, testified about such resistance to

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339/ Glueck, Exit the Drugstore Unless . . . in L. BOONE (ed), MARKETING CHANNELS 455 (1973).

340/ *Id*. at 456, citing DRUG TOPICS, January 12, 1953. Pharmacists have also attempted to eliminate price competition by preventing the advertising of prices. Such prohibitions are implemented either by state regulation or rules of "ethical conduct" administered by pharmacy boards. Both restrictions are currently under legal challenge, with state regulations being challenged in an FTC rulemaking, 40 FED. REG. 24031 (1975), and with the Antitrust Divisionbringing suit to enjoin the use of such ethics codes. United States v. American Pharmaceutical Ass'n, Civ. No. G75-558, W.D. Mich.

change in the cooperative association of independent grocers in Washington, D. C., an organization of which he previously had been president: 341/

> I left because I felt there was no future in District Grocery Stores. The membership refused to accept the fact that the small grocery store was becoming obsolete as the vast majority of consumers demanded variety which it is impossssible for the small store to provide. History has proven me correct as DGS discontinued business two years ago. The point is simply that the small retail grocer goes out of business not because of product cost but instead is a casualty of changing market conditions.

Mr. Fox indicated that in contrast to the situation in the Washington area, where the grocery store members had refused to change to larger stores and to build a modern warehouse, the Kansas City cooperative of which he is now president had built a modern warehousing operation and was able to convert many willing small businessmen from small grocery store proprietors to owners and operators of larger, independent supermarkets.

c. Existing Evidence Shows That Robinson-Patman Accomplishes Little To Protect Small Businesses as a Group

As noted at the outset of this Report, there are few direct economic studies which can precisely determine the costs and benefits of Robinson-Patman to the nation. However, evidence does exist which strongly tends to confirm the analyses presented in this section showing that Robinson-Patman has little effect on the overall ability of a small business to survive. First, is the example of the Associated Wholesale Grocers Cooperative in Kansas City. That cooperative covers over 500 grocery companies in Kansas, Missouri, Arkansas, Oklahoma, Nebraska, and Iowa. Its membership includes a large national chain, a chain of convenience stores, independent chains

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341/ Testimony of Louis Fox, DCRG Hearings, Tr. 90-91.

having twenty supermarkets, and independent corner grocery stores having one location. The latter comprise 40 percent of its members. Because of the organization's history as a cooperative, all members large and small are charged the <u>same</u> price for all their purchases, plus the actual cost of transportation. This is the cooperative's policy even though it costs <u>substantially</u> <u>more</u> to process the order of the small grocery store since the order contains relatively fewer items but the "picker" must traverse the whole area of the warehouse to select all the items. 342/

But as Mr. Fox testified, even this extraordinary cost equalization cannot save the small operation: 343/

> nothwithstanding our efforts to properly serve small stores, the attrition rate is substantial. Specifically, during the year 1974 our records reflect that 27 of the small independents terminated their business. If we have 197 small stores now and they go out of business at the rate of 25 stores a year, how long will it be before they are no more?

Mr. Fox indicated that the smaller stores were going out of business because they simply did not meet the needs of the buying public. Fox concluded: 344/

> With the factual evidence presented to this council, I believe there is no doubt that the Robinson-Patman Act must be modified if the free enterprise system which made this country the envy of the free world is to work again. Over-regulation on the part of government is not only increasing the budget but causing productivity to decrease while raising the nation's rate of inflation.

342/ *Id*. at 86, 101-03, 106, 112.

343/ *Id*. at 90.

344/ *Id*. at 93-94.

My concluding point is that times change. One can't stand still. Either we adjust to accommodate change or we go backwards. The downward trend of the small corner grocery store will not change as today's consumer demands increased variety which is impossible for the small stores to provide. Likewise, I ask that you recognize the changing distribution pattern which has evolved gradually in this country, but is distinctly different from what existed 39 years ago when the Robinson-Patman Act was created . . . . But if the Federal Government does not aggressively move to change their laws as necessary to satisfy the changing times, our country will not remain for long the leader of the free world.

A comparison between small businesses and the percentages of sales attributable to small businesses in the United States and Canada is also quite revealing. Canada does not have any civil antitrust law dealing with price discrimination. It does have a criminal statute 345/ which deals with price discriminations and discriminatory promotional allowances. The section of the statute dealing with price discriminations, however, requires the discriminatory sales to be not only of "like grade, and quality" but also of "like quantity" thus making the statute relatively meaningless. There apparently have been no criminal prosecutions under this statute and obviously the Act cannot be enforced by private persons. Thus, for all intents and purposes, Canada is without a statute like Robinson-Patman.

Canada's retail trade is relatively similar to that of the United States in that it is composed of independent small businesses and large chains. Therefore, meaningful comparison between Canada's small businesses and those of the United States can be made. Defining "small business"

345/ 1971 Rev. Stat. Can. Ch. C-23 §§ 34, 35.

to mean a retail firm having only one place of business, one finds these results in examining the following numbers (derived from tables 1-3):

Comparison of Small Firm Performance in Canada and the United States

	Percent of Retail Sales		Percent of Establishments	
	U.S. 1967	Canada 1966	U.S. 1967	Canada 1966
Overall	60.2	61.8	87.5	87.4
Grocery Stores	38.9	41.6	84.6	81.2
Drug Stores	61.0	76.5	83.5	81.7

Thus, as measured by the number of stores the overall position of the small retailer in both economies is almost identical. In the area of groceries, and particularly drugs, the proportion of sales volume represented by the smaller firms, however, is less in the United States.

Because there may be some regional disparities between the United States and Canada as a whole, comparison was also made of the position of small businesses in the Province of Ontario and the State of Michigan. On the basis of the percentage of sales, small businesses in Ontario captured 58.2 percent of the sales, and in Michigan 56.9 percent. On the basis of the number of stores operated, in Ontario small businesses had 83.9 percent, and Michigan 86.7 percent. Again, the similarities are striking.

Thus, from these figures, it seems impossible to conclude that Robinson-Patman has had any effect on the number of small businesses. On the contrary, it probably has not. The important thing to remember is that in the United States with Robinson-Patman, chains comprise a greater proportion of retail sales than they do in Canada without Robinson-Patman.

In comparison to "fair trade," Robinson-Patman has relatively limited ability to affect the competitive relationship between larger and smaller

TABLE 1

Position of Single Stores in Retail Lines of Business

U.S. 1967

Line of Business (SIC)	($ Million) Sales of Single Stores	Per Cent of Total	Number of Single Stores as Per Cent of Total Stores
Total	$186,709	60.2%	87.5%
Grocery Stores (541)	25,301	38.9	84.6
General Merch. Group Stores (53)	5,809	12.8	67.1
Tire, Battery & Accessory Dealer (553)	2,386	56.3	77.5
Gasoline Service Sta. (554)	18,945	83.4	89.2
Apparel & Access. (56)	8,623	51.7	73.7
Hardware (5251)	2,426	86.2	94.4
Furniture (5712)	4,701	71.6	87.6
Household Appliance (572)	1,926	63.9	73.0
Drug Stores (591)	6,662	61.0	83.5

Source: 1967 CENSUS OF BUSINESS, Table 4-1.

TABLE 2

Position of Single Stores in Retail Lines of Business

Canada 1966

Line of Business	($ Million) Sales of Single Stores	Per Cent of Total	Number of Single Stores as Per Cent of Total Stores
Total	$14,022	61.8%	87.4%
Grocery Stores with fresh meat	1,845	41.6	81.2
General Merch. * Group Stores	621	37.6	81.0
Tire, Battery & Accessory Dealers	230	71.0	81.3
Service Stations	1,549	92.7	95.7
Apparel & Accessory Stores **	765	57.9	72.1
Hardware Stores	272	76.1	92.1
Furniture Stores	264	71.2	80.1
Household Appliance Stores	76	65.5	75.6
Drug Stores	496	76.5	81.7

(Notes and source on next page).

Source: 1966 Census of Canada -- Retail Trade, Size of Business, Table 11, pp. 11-1, 11-2 (1969).

* Includes General Merchandise Stores, General Stores, Variety Stores.

** Men's & boys, women's & misses', family, shoe stores.

TABLE 3

Single Stores' Position in Ontario (1966) and Michigan (1967)

	Sales of Single Stores ($ Million)	Per Cent of Total	Number of Single Stores	Per Cent of Total
Ontario	$5,024	58.2	42,873	83.9
Michigan	8,024	56.9	55,128	86.7

Source: 1967 CENSUS OF BUSINESS, Table 4-3; 1966 CENSUS OF CANADA--RETAIL **TRADE, SIZE OF BUSINESS, TABLE 11, at 11-13 (1969).**

retailers. Thus, an analysis of the effectiveness of fair trade is quite relevant to analyzing the effectiveness of Robinson-Patman.

"Fair trade" did not merely attempt to assure that businessmen would have the same price for their costs of goods to be sold. Rather, fair trade mandated a uniform retail price. There was no justification for a lower price, and neither efficiencies of distribution nor efficiencies in the actual operation of a retail establishment could result in a large store charging a lower price. More importantly, by preventing the larger store from lowering its price as a result of lower service levels provided to the consumer, fair trade deliberately attempted to preserve a service/price ratio that favored smaller businesses. Former Assistant Attorney General Donald Turner agreed that the repeal of resale price maintenance to the extent that it had an effect on small businesses "would have a greater destructive impact on the existence of a larger number of small competitors than the repeal of Robinson-Patman." Turner continued: 346/

> [J]ust look at what Fair Trade does. I mean, under fair trade says -- when you have effective fair trade, by and large the minimum price is set high enough to permit a relatively small store with low turnover to survive. It is a margin problem. The way it sort of comes out, the advantage the big store has over the small store is rapid turnover -- they can operate on a much narrower margin than the small store does with a slow turnover. And if you suddenly lift Fair Trade and allow a store which can make a profit on a ten - twenty percent markup to price accordingly, that is fatal to the store -- well, it is not necessarily fatal, but it certainly has a devastating impact on the store that has to charge forty - to fifty percent markup in order to survive. . . .

346/ Testimony of Donald Turner, DCRG Hearings, Tr. 326-27.

> But, surely, in terms of impact it just seems to me to be obvious that to subject stores to the competition of more efficient retailers has much more devastating impact than to enable large chains, say, to get a ten percent break on the price of the commodity, the commodity cost being only a small part of the cost of total operation. And by the time you pass that through to the retail price, it is an even smaller fraction than it is there. Just in terms of magnitude of a potential impact, they are much different.

Yet, several recent studies have demonstrated that "Fair Trade" did not, in fact, lead to any significant protection of small businesses. It was partly on this basis that Congress recently voted to repeal the exception to the antitrust laws which permitted states to pass fair trade statutes. 347/ As the House Report on the legislation to repeal fair trade stated: 348/

> The principal traditional justification for 'fair trade' laws has been that they protected small family-owned retail outlets -- the 'Mom and Pop' stores -- from price gouging by the discount chains. Proponents of this view argued that these independent retailers frequently provide on-going service of the product and individual attention to the customer's needs, which add to their overhead and prohibit them from competing effectively in price with the chain stores.
>
> The first difficulty with this argument in it is that it finds no real support in the facts. A well known 1965 study of small-business failure rates between 1933 and 1958 did not show that such firms fared any better in 'fair trade' States. To the contrary, the study by Dr. Stuart Lee of Geneva College found a higher rate of small business failures in 'fair trade' States without such laws. Other studies by the Department of Justice and the Library of Congress, the latter in 1972, confirmed that the 'fair trade' states actually show higher small business failure rates. The growth rate of small businesses between

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347/ Pub. L. No. 94-145, 89 Stat. 801.

348/ H. Rep. No. 94-341, 94th Cong., 1st Sess. 4-5 (1975).

1956 and 1972 were 32 percent higher in non-"fair trade" states. Moreover, studies conducted in places which have abandoned resale price maintenance show no adverse effect on small businesses. Experience in Rhode Island, which repealed "fair trade" in 1964, Canada, which repealed it in 1957, and Great Britain which stopped "fair trading" in 1965, indicates generally lower prices, more business competition, and no adverse effect on small businesses.

Finally, the performance of small firms in the unregulated service industry sector supports the conclusion that the existence of a price discrimination statute is not necessary to the survival of small firms and the maintenance of competition. The Robinson-Patman Act applies to the sale of "commodities" in interstate commerce and does not therefore prohibit price discrimination in the sale of services. Yet, as one witness before the Review Group testified, service industries constitute one of the least concentrated sectors of the economy (Testimony of Kenneth G. Elzinga, DCRG Hearings, Tr. 264-65).

3. Robinson-Patman Does not Achieve Significant Competitive Goals

Even though Robinson-Patman cannot protect small business as a class, the statute would provide benefits to society if it promoted the long-run antitrust goals of ensuring lower prices through reduced concentration and if it protected smaller businesses from truly predatory actions while enabling them to counter the buying power of larger businesses. But rather than being a true antitrust law, the Act effectively is a regulatory statute. The adverse results are inherent in Robinson-Patman's role as an incipiency statute based on price discrimination. Moreover, the information available to the Review Group shows that Robinson-Patman does not prevent increased concentration in any meaningful way and that the repeal of the Act would not lead to any long-run losses in consumer welfare. Similarly, other procompetitive ways exist to protect small businesses from predatory activity while enabling aggressive small businessmen to counteract the buying leverage of larger firms.

a. Consistent With Its Origins, Robinson-Patman Was Drafted, Not as an Antitrust Law Designed to Protect Competition, But as a Regulatory Law Designed to Protect Classes of Businesses

The essential provisions of the Robinson-Patman Act are, as a matter of law, amendments to Section 2 of the Clayton Act, which itself is an antitrust statute. Because of this fact, proponents of Robinson-Patman steadfastly maintain that it is not a regulatory statute, but an antitrust law. Those who are critical of the statute, on the other hand, maintain that the statute, apart from its location in the United States Code, is essentially nothing more than a regulatory law, and is in total contradiction to more important goals that are generally ascribed to antitrust statutes. The reason why these two diametrically opposite positions are held, and held with genuine conviction by participants in the Robinson-Patman debate, is that it is theoretically possible to ascribe to Robinson-Patman goals which are in accord with the antitrust laws. At the same time, it is also equally possible to point out its anticompetitive -- and hence non-antitrust -- effects on actual business practice.

The antitrust laws, as they are embodied in the bulk of the Sherman and Clayton Acts, have as their goal the enhancement of consumer welfare by promoting the maintenance of competitive markets and actual competition, primarily on price. They do so by making unlawful two types of business conduct. Generally speaking, the first type is composed of inter-business agreements which are in restraint of trade. These agreements, such as price-fixing agreements and territorial or customer allocations, represent agreements among competitors not to compete or agreements among suppliers and customers which have the effect of foreclosing competitive opportunities in the economy. The second type of proscribed activities are those which involve actual or attempted changes in the structure of the market which may have serious anticompetitive effects. These activities, monopolization, attempted monopolization, or mergers of a type which seriously reduce the prospect of competition in a given line of commerce, are forbidden because they are not the product of, or do not represent the continuation of, genuine competition on the merits. If allowed to go unchecked, they would result in the actual reduction of competition in the marketplace and less efficient utilization of society's resources.

The problem with Robinson-Patman is that the theoretical anti-trust goal which could be assigned to a "pure" version of Robinson-Patman, i.e., preventing powerful buyers from exacting non-cost justified discounts and thus from injuring more efficient competitors of the buyer, cannot be achieved as a practical matter without conflicting with the other antitrust goal of preserving vigorous and flexible price competition for new customers. In other words, Robinson-Patman reaches the goal of protecting more efficient competitors by pricing restrictions which, if agreed to by, say, an association of small businessmen and their suppliers, would be per se violations of the Sherman Act. Such agreements would both insure high prices to the sellers, particularly if they were oligopolists, and prevent competition for buyers. One witness before the Review Group, Professor Donald Turner, a former Assistant Attorney General in charge of the Antitrust Division, conceded the theoretical antitrust rationale for Robinson-Patman, but pointed out that the theoretical goal could not be attained without collision with other antitrust goals: 349/

> Now, there is this difference about Robinson-Patman, and I think in all candor it should be conceded. There is an economic rationale for that aspect of the Robinson-Patman Act that attempts to protect small buyers against true discriminatory prices, that is, price differences unrelated to the cost, a rationale which Fair Trade lacks.
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> From an economic standpoint, competition, say, at the retail market would work satisfactorily only if the various competitors in that market were not suffering from competitive disadvantages related to their relative efficiency. Now, in the strict sense, if a small buyer has to pay more for the goods that he resells simply because he is small, it has nothing to do with cost savings on the part of the seller and is an unfair advantage.
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> If it were possible to eliminate that unfair disadvantage without ill effects of another sort, then I think legislation of this kind would be justifiable. The problem is that you cannot.

349/ Testimony of Donald F. Turner, DCRG Hearings, Tr. 307-08.

Unlike a "pure" Robinson-Patman, concerned only with the preservation of competition, the real Robinson-Patman Act is explicitly directed toward the protection of individual businessmen. Under the Act, Congress has singled out two major beneficiary classes, small businessmen and enterprises performing the wholesale function. The appropriate governmental agencies are charged with insuring that these classes are not treated "unfairly" in the operation of the dynamic competitive processes that characterize the marketplace.

It is precisely this function, the regulation of price competition -- direct and indirect -- for the benefit of certain favored incumbents in an industry, which (along with entry regulation) characterizes the essence of economic regulation as it has developed in the American system. The Interstate Commerce Commission has as its function the regulation of pricing among truck lines to prevent "destructive competition" and to govern the competitive relationship between railroads, trucks, and water carriers. The Civil Aeronautics Board controls the rates and competitive relationships among air carriers. The Federal Maritime Commission has as its basic function the approval and oversight of the competitive relationships in price among ocean carriers. The Securities and Exchange Commission, until 1975, controlled the competitive rate structure among securities brokers. The Federal Communications Commission is attempting to regulate the competitive relationships between over-the-air broadcasters and cable systems. And the Federal Energy Administration, as part of its overall control over petroleum, has established an elaborate system of payments among petroleum refiners so as to equalize the competitors' cost of petroleum purchased and thus counteract the effect of FEA controls on crude oil prices.

A clear example of Robinson-Patman's "regulatory mentality" can be seen in the courts' handling of the issue of whether a firm may charge below its fully allocated cost, or its lower variable cost, before being found guilty of predation. In the Utah Pie case, discussed extensively above, 350/ the Supreme Court found that the sale of a commodity below an accountant's definition of fully allocated cost was predatory even though the sale remained above variable costs for serving the particular community. Such a standard is designed to *protect* the small single-product, and/or single-location firm from competition by larger firms which are able to cover their overhead costs on several product lines or in several areas. A trial court has also clearly articulated Robinson-Patman's regulatory objective in connection with pricing or accounting practice: 351/

350/ See text at note 20 , *supra*.

351/ William Inglis & Sons Baking Co. v. ITT-Continental Baking Co., No. C71-1906 SW, N.D. Cal., Jan 21, 1975, Slip Opinion at 15-17.

> Assume for the purpose of this illustration that a multi-product company is in competition with a single-product company. In such a situation, the multi-product company using the variable cost method could allocate major indirect cost items reduced proportionately to a non-bread line, and allocate little or nothing to his bread products. Accordingly, he could claim "costs" far below those his single-product competitor could claim and set prices above his "cost" that his competitor could not meet without suffering losses. Even though the multi-product competitor could claim overall "profitability" the resulting damage to competition -- and the bread market -- is self-evident.
>
> Accordingly, it is the view of this Court that any costing method that does not allocate both the direct cost to the specific product and the fair share of the total overhead to the product is so fraught with the opportunities for abuse to be acceptable [sic] for the purpose of Robinson-Patman . . . cost determinations.

Note that in these decisions, the courts never determined which of the firms in the market had the lower variable cost, i.e., which could produce the product most efficiently.

The Interstate Commerce Commission has historically faced the same problem: whether railroads may lower their rates to the variable cost level in order to compete with trucks or barges. Of course, the overhead cost for a railroad includes the cost of maintaining the railroad's roadbed and right-of-way, costs which neither barges nor trucks have to bear. Nevertheless, the Interstate Commerce Commission has traditionally prevented railroads from pricing on the basis of marginal cost for precisely the same reasons underlying Robinson-Patman. Thus, in one case denying a railroad the right to lower its rates the ICC stated: 352/

352/ Grain in Multiple-Car Shipments - River Crossings to the South, 321 I.C.C. 592, 597 (1963).

> Even though the fully-distributed [fully allocated] cost standard is marred by theoretical and practical infirmities, it has been instrumental in preserving the inherent advantages of carriers whose traffic repertoire is so limited that they cannot afford to transport several of their most important commodities at less than the full cost of performing the service.

Similarly: 353/

> . . . regulation could be neither fair nor impartial if we did not recognize the fact that the carriers before us do not compete for every type of traffic. It is quite obvious, for example, that the traffic here involved is of far more consequence to the barges than to the railroads. . . . In short, an inherent cost advantage under the national transportation policy reasonably could not embrace a concept that would impair the ability of a carrier not only to compete, but to exist.

That this standard was purely protectionist and was not economically sound was clearly recognized by at least one ICC Commissioner: 354/

> Most economists and accountants seem to agree that fully-distributed costs represent the result of an effort to allocate certain costs which by definition cannot be allocated to particular service units. There is no doubt in my mind that such fully-distributed cost constructions are bottomed on economic fallacy. . . . One of the great paradoxes in transport regulation is that this form of economic nonsense, in view of the disparate cost structures of competing modes, may be entirely sound from a regulatory point of view.

It should be noted that in the recently passed Railroad Revitalization and Regulatory Reform Act 355/ Congress reversed this protectionist attitude according presumptive legality to railroad tariffs which covered variable costs.

353/ Ingot Molds, Pennsylvania to Steelton, Ky., 321 I.C.C. 77, 82 (1965). (Emphasis added)

354/ Remarks of Comm. Charles Webb before the National Accounting and Financial Council of the American Trucking Associations, May 13, 1963, quoted in Brief of Respondent Railroads to ICC Division 2, Ingot Molds, at 23 (1965).

355/ Pub. L. No. 94-210, 90 Stat. 31.

Protectionism is all the more evident in secondary line situations where the expressed purpose of Robinson-Patman's sponsors was to prevent businessmen from freely bargaining over price with their suppliers if competing small purchasers were unable to bargain as effectively. Once a protectionist mandate is given to an administrative agency, the concern over relationships among competitors and "equality of opportunity" soon becomes transmuted into the characteristic regulatory goal of insuring against the financial failure of the firms and the industry it regulates. Such concern is, for example, explicitly set out in the rate standards which the Civil Aeronautics Board uses in setting carriers' rates: the need of each firm "for revenues sufficient to enable such air carrier, under honest, economical, efficient management, to provide adequate and efficient air carrier service." 356/

It is not surprising, then, that an appeals court found that the Federal Trade Commission in administering the Robinson-Patman Act, appeared to operate under the belief that Robinson-Patman "was intended to freeze prices at the level which would return a profit to a competitor in a market with the highest costs." 357/ Like the ICC, Robinson-Patman thus serves as a "giant handicapper" 358/ of particular businesses. This objective also is quite similar to those of the extensive Federal

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356/ 49 U.S.C. § 1482(e)(5).

357/ Dean Milk Co. v. FTC, 395 F.2d 696, 701 (7th Cir. 1968).

358/ ICC v. New York, N.H., and Hartford R.R., 372 U.S. 744, 758 (1963).

Milk Marketing Order regulatory scheme, i.e., to insure an "adequate supply" of milk and enhance producer income. 359/

The ability of businesses to commence judicial treble damage and injunctive actions to forestall the lowering of prices to or by their competitors gives Robinson-Patman a striking similarity to another aspect of regulatory statutes: the invocation of government power to promote uniform pricing practices. Under ICC practice, for example, attempts by individual motor carriers to decrease rates are usually met by a series of complaints to the Commission by competing carriers that the rates are "unjustly and unreasonably" low. The resulting Commission proceedings on such complaints, regardless of the ultimate validity of the rates, act as an inhibiting factor on the freedom of individual carriers to reduce prices and strengthens parallel pricing in the industry. The ICC has recognized, in part, the seriousness of this problem and has recently promulgated regulations designed to reduce the ability of "rate bureaus" of competing carriers to protest the rate filings of individual trucklines. 360/ The rise in private Robinson-Patman litigation, on the other hand, may foreshadow increased recourse to the Act as a means of achieving government-induced price stability.

Finally, the administration of Robinson-Patman exhibits the same key characteristics as that of other clearly regulatory statutes, that is, the existence of detailed administrative rules guiding the type

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359/ 7 U.S.C. §608c; 7 C.F.R. Subtitle B, ch X.

360/ Rate Bureau Investigation, 349 I.C.C. 811 (1975), 351 I.C.C. 437, 460 (1976).

of activity a businessman may engage in lawfully. The Code of Federal Regulations, Title 16, contains many pages of Federal Trade Commission advisory opinions and guidelines concerning the legality of various pricing and promotional allowance practices. Perhaps the most onerous from a business standpoint are the various advertising allowance regulations contained in the so-called Fred Meyer Guides for promotional advertising allowances. 361/

Of course, once a businessman wants to do something that may be questionable under these guidelines, or indeed feels that these guidelines are unjust and would like to see them changed, he may feel it prudent to petition the agency for clarification or for advice. Such advice may take a long time to fashion, leaving the businessman very much in a quandary as to what to do. In recent testimony before Congress, Federal Trade Commission staff revealed that several requests for clarifications relating to the Fred Meyer Guides filed over two years earlier had not been acted upon. 362/ Also, caution extends to business practices which are subject to outstanding Federal Trade Commission orders, most of which are of infinite duration. In such cases, businessmen may actually feel compelled to request FTC approval before putting into effect a change in their pricing structure. 363/

361/ 16 C.F.R. pt. 240.

362/ Testimony of Bartley T. Garvey, Subcommittee Hearings, pt. 2 at 197.

363/ Testimony of FTC Comm. Mayo Thompson, Before the Joint Economic Committee, November 18, 1974, at 8.

Hence, the Robinson-Patman Act, as it is written and as it is enforced, is in reality a regulatory statute: it is designed to control the competitive relationships among businesses without an overriding concern for the promotion of consumer welfare; it is administered with a concern for the continued financial viability of existing firms in the marketplace; and it imposes on individual businessmen -- particularly smaller businessmen who do not have corporate counsel -- the burden of high legal expenses and agency interference in their marketing decisions. In actual practice, then, the theoretical antitrust concerns of Robinson-Patman are submerged by other "regulatory" goals.

b. The "Incipiency" Test of Robinson-Patman, Unlike That of Section 7 of The Clayton Act, is Ill-Suited to Achieving Antitrust Goals

One of the basic premises of supporters of Robinson-Patman is that the Act can serve a useful antitrust role by preventing practices which may result in the establishment of market dominance by one -- or a very few -- firms without the necessity of awaiting the actual achievement of such market power. In this respect, Robinson-Patman is meant to serve the same function as Section 7 of the Clayton Act, dealing with mergers. The intent of such a statute was concisely expressed in the Congressional record dealing with the 1950 Amendments to Section 7: 364/

> The intent here . . . is to cope with monopolistic tendencies in their incipiency and well before they have attained such effects as would justify a Sherman Act proceeding. (Senate Report)
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> Acquisitions of stock or assets have a cumulative effect, and control of the market . . . may be achieved not in a single acquisition but as the result of a series of acquisitions. The bill is intended to permit intervention in such a cumulative process when the effect of an acquisition may be a significant reduction in the vigor of competition. (House Report)

Or as one Robinson-Patman sponsor put it: The purpose of Robinson-Patman is to "catch the weed in the seed [to] keep it from coming to flower." 365/

Incipiency statutes serve a useful public function when they are actually able to prevent market dominance by one -- or a very few --

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364/ Brown Shoe Co. v. United States, 370 U.S. 294, 317 n. 32 (1962).

365/ S. REP. No. 1502, 74th Cong., 1st Sess. 4 (1935).

firms, while at the same time not discouraging pro-competitive business activity. The fundamental problem with Robinson-Patman, particularly as applied to the secondary-line cases, is that as a statute which utilizes the presence of price discrimination as the key indicia of an incipient antitrust violation, the Act inherently outlaws a substantial volume of procompetitive price reductions.

Even in its pure form, referring only to injury to competition, and not to individual competitors, an incipiency test requires that courts decide whether the effect of the questioned action "may be substantially to lessen competition" in the relevant market. As the Supreme Court has recognized, such a question: 366/

> is not the kind of question which is susceptible of a ready and precise answer in most cases. It requires not merely an appraisal of the immediate impact of the [activity] upon competition, but a prediction of its impact upon competitive conditions in the future . . . . Such a prediction is sound only if it is based upon a firm understanding of the structure of the relevant market; yet the relevant economic data are both complex and elusive.

Because those deciding proceedings brought under an incipiency statute have to make prospective determinations regarding the actual impact of a particular transaction, they must employ logical inferences about the probable effect of the questioned activity on a given market. The degree of speculation inherent in such inferences differs according to the activity subject to statutory scrutiny. Deciding

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366/ United States v. Philadelphia National Bank, 374 U.S. 321, 362 (1963).

whether price discrimination is anticompetitive necessarily involves a faulty inferential process while making similar decisions with respect to mergers does not.

A determination that a particular activity is unlawful under an incipiency statute dealing with pricing behavior, such as Robinson-Patman (in contrast to a statute dealing with actual structural changes such as mergers) must result from a cumulation of inferences: First one must infer that the existence of a pricing practice will lead to structural change in the market, i.e., the exit of one or more competitors. Second, one must make the further inference that the structural change resulting from the elimination of one or more competitors will have an adverse impact upon competition in that market.

Testing the validity of such inferences on a case-by-case basis would be inordinately complex, speculative, and time consuming. Moreover, the outcome of such an investigation, requiring the work of many economists, statisticians, and lawyers, could not possibly be known to any of the businesses involved in that marketplace prior to the outcome of the fact-finding proceeding in the case. The business community, however, has an overriding concern in knowing the lawfulness of a proposed pricing activity before it is carried out. The need for such guidelines is greater here than in the case of Section 7; while mergers occur but very infrequently among businesses, prices are set every day and there is much less opportunity to devote a great deal of time to analyzing the societal impact of each price a businessman may wish to charge. Moreover, the maintenance of pricing flexibility is the paramount objective of the antitrust laws.

The agencies enforcing Robinson-Patman have recognized this need for guidelines, and have thus felt it appropriate to establish a set of presumptions as to when the inference of structural change from a price discrimination, and the inference of anticompetitive effects from a structural change, may be drawn in the absence of strong countervailing evidence. The standard that the Supreme Court has approved in secondary-line cases -- the Morton Salt test -- is that the requisite potential for competitive harm will be shown when, in a market characterized by low profit margins, a price discrimination is sufficient in amount to affect the resale price for the commodity. 367/ The logical inference is that a difference significant enough in amount to affect the resale price in such a market could cause customers to switch stores if the disfavored purchaser did not lower his price, or could cause the seller to sell a price at or below cost, if he decided to meet the price of his competitor. Various types of evidence tending to rebut this inference have been held irrelevant. 368/ For instance, the fact that the discriminated item is only one of a very many items a retailer sold is deemed of no importance: 369/

> There are many articles in a grocery store that, considered separately, are comparatively small parts of a merchant's stock . . . . Since a grocery store consists of many comparatively small articles, there

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367/ FTC v. Morton Salt Co., 334 U.S. 37, 45-49 (1948).

368/ See text at 12-14.

369/ Id. at 49.

is no possible way effectively to protect a grocer from discriminatory prices except by applying the prohibitions of the Act to each individual article in the store.

The Act thus has made presumptive the following series of inferences: 1) if any price discrimination is permitted, the practice will become generalized, 2) if the practice becomes generalized and a merchant has to pay discriminatorily high prices for all, or almost all, of the commodities he purchases for resale, he would be forced out of business, and 3) if similarly-situated disfavored purchasers were forced out of business, then the structural change would be severe enough to affect the competitive vigor of the remaining firms in the market.

There are two basic problems with such a series of presumptions. The first is that such presumptions are both anticompetitive and untrue. The second is, they are probably essential to practical enforcement of the Act. As for the first problem, this Report has previously demonstrated at length that the use of broad presumptions in establishing a prima facie case leads to needless pricing caution and other anticompetitive results. These harmful effects occur because an incorrect invocation of the presumption results in direct harm to competition through improper interference with the price-setting mechanism, and probable injury to the ultimate consumer through elimination of the opportunity to receive goods at a lower price. At the same time, the evidence available to the Review Group does not demonstrate that in the absence of Robinson-Patman, prices to smaller businesses would be so pervasively higher as to drive most small businesses out of the market, nor does it show that the reduction of those small businesses which in fact might exist would be so significant as to impair seriously the competitive vigor of a given market. The presumption that a price discrimination large enough to cause a difference in resale price will ultimately result in injury to competition and the consumer is thus invalid also -- except in entirely fortuitous circumstances. Consequently, the use of such presumptions has the effect -- just the reverse of the Sherman Act -- of making many individualized price reductions per se unlawful.

This result is in sharp contrast to a statute, like Section 7 of the Clayton Act, whose incipiency test is based on structural change rather than pricing behavior. Under Section 7, the courts' presumptions about the likely effect of challenged mergers do serve a useful antitrust function: Courts and the FTC look at the relevant "lines of commerce" and the marketplace, and decide whether the increased market concentration resulting from that merger alone, or from the cumulative effects of a series of similar mergers would be likely to produce oligopolistic or monopolistic behavior in the market. In such a process, courts presume that competitive behavior, particularly competitive pricing, will be unreasonably diminished in highly concentrated markets. Just as importantly, mergers, unlike price reductions, are not an essential part of the competitive process, and the mere fact that a merger is taking place, reflecting as it may the operation of our tax laws or the securities markets, does not necessarily signal the achievement of any benefits to the public at large. Thus, the Supreme Court could appropriately conclude in establishing permissible presumptions in Section 7 cases: 370/

> 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 [citation omitted].
>
> Such a test lightens the burden of proving illegality only with respect to mergers whose size makes them inherently suspect in light of Congress' design in §7 to prevent undue concentration. Furthermore, the test is fully consonant with economic theory. [citation omitted]

Additionally, the relatively few number of mergers, compared to the billions of pricing decisions, permits much more careful case-by-case economic evaluation of a merger's competitive effects, and less anticompetitive alternatives to it.

Unfortunately, the presumptions which have been adopted by the courts in deciding Robinson-Patman cases are probably necessary to the meaningful administration of the statute. If Robinson-Patman is to serve as a statute dealing with alleged incipient threats to competition, claimed violations of the Act must be adjudicated without waiting to see if their effect is to decrease competition. A statute that outlawed only pricing practices which actually had the effect of increasing concentration and reducing competition is possible, but it would not be an incipiency statute like Robinson-Patman.

Because it is not possible to administer Robinson-Patman through elaborate economic proceedings to determine whether complained

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370/ United States v. Philadelphia National Bank, 374 U.S. 321, 363 (1963) (emphasis added).

of discriminations actually will have a serious impact on market structure, those enforcing the Act must make certain presumptions about their potential anticompetitive impact. If those enforcing the Act were to make the presumption that arises from actual experience, they would presume that in the substantial majority of cases, price discrimination on the secondary line does not result in significant enough structural change to threaten adverse competition consequences. But such a posture would mean few Robinson-Patman cases could ever be successfully brought. Consequently, if Robinson-Patman is to have any operative effect, those deciding cases under it must assume that the presumptions of requisite harm are valid, even if, in fact, they are not.

In sum, failure to utilize the Morton Salt presumptions in an incipiency statute based on price discrimination would result either in non-enforcement of the law or in extreme business uncertainty and caution in pricing. Utilization of such presumptions, though, results in the condemnations of pricing actions which if left unchallenged would not, in fact, result in any significant competitive harm. This dilemma of Robinson-Patman seems incapable of solution.

c. There Is No Evidence That Repeal of Robinson-Patman Would Lead in The Long Run to Significantly Increased Concentration And Higher Prices

A key argument of Robinson-Patman proponents is that the Act in the long run helps consumers. The argument is made that any price reductions created by more short term vigorous competition among buyers are outweighed by the prospect that such lower prices will drive smaller merchants out of the market, thereafter giving the larger merchants a license to raise prices to a higher level than before.

As discussed in Section A, 371/ of this Chapter, where sellers have market power, prices are often higher than those which would be set in a competitive market. One of the most effective ways to reduce high, oligopolistic, prices is the exercise of countervailing buyer power to obtain price concessions. If the concession cannot be made to those in a strong bargaining position, but must be made on an all-or-nothing basis, the likely outcome is that no price concession will be made and prices will remain high. Proponents of Robinson-Patman argue that any lower prices obtained by the consumer from such bargaining advantage would be a "fool's paradise" leading, as the small merchant disappeared, to prices high enough to outweigh the lower prices which would occur in the initial period following the Act's repeal. This would result if the absence of Robinson-Patman would decrease the competitive nature of retailers and would lead to the establishment of high oligopoly prices in that market.

371/ See text at page 156, *supra*.

There is no evidence to support the argument made by Robinson-Patman proponents that unleashing buyers in price negotiations would ultimately bring harm to consumers. Indeed, the evidence points to an opposite conclusion. In order for such bargaining flexibility to have an adverse long run impact on consumers, four conditions must exist. First, the price reductions obtained by a purchaser with bargaining leverage must never become generalized throughout the industry. Second, lower prices based on a uniquely lower cost of goods purchased must cause the elimination of several weaker but competitively significant rivals, thus strongly increasing the oligopoly power of the purchaser. Third, the favored purchaser, after the elimination of several of its competitors, must raise its prices not merely to the level that existed before the firm received its price advantage, but to a higher level. If prices rise only to their pre-discrimination level, consumers are no worse off than if no discount had been allowed. In fact they are better off because in the interim they would have received lower prices. Fourth, post-discrimination high oligopolistic prices must be maintained for a long enough period to outweigh the savings obtained by consumers during the previous period of vigorous price competition.

The evidence available to the Review Group demonstrates that such a series of events is quite unlikely. With respect to the first necessary condition, that the lower prices will not become widespread, most witnesses before the Review Group stated, to the contrary, that once a price cut becomes known, -- and it usually becomes known because the lower price results either in a lost customer or in a lower resale price -- the movement in the industry is towards a general reduction of prices from higher oligopolistic levels. In such a case, the temporary exclusive benefit of the recipient of the price cut becomes a general benefit to all as manufacturers' prices fall. On the other hand, if the favored purchaser does not switch suppliers, or if he does not lower his resale price, the price discrimination may indeed remain unknown for some time. Of course, if the purchaser does not lower its resale price, then there is no harm to any of its competitors since without the price reduction, there will be no diversion of customers. The only result is that the favored purchaser makes higher profits on the sale of that item, that is, he obtains part of the oligopoly profits that would have accrued to the manufacturer.

Most sectors of the retail industry are quite competitive. One witness before the Review Group, Mr. Douglas Wiegand, of the Menswear Retailers of America, evidenced this competition by his observation that "Retailing has historically been a low profit, low return on investment industry." 372/ Mr. Wiegand thought that in spite of this competition, demonstrated by the low rate of return, any price discounts would not be passed on: 373/

> Apart from possibly emasculating small business, we believe that the RP trade-off would be higher profits to a few giants and not lower consumer prices. . . . What these giant corporations have been doing is focusing in on before taxes profits of 5 percent and 6 percent. With RP off the books why shouldn't they shoot for 8 percent or 10 percent rather than pass the savings on to consumers ?

To the extent that this result is true, there would be no "emasculation" of smaller businesses because if prices were not lowered, there would

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372/ Prepared Statement at 7, DCRG Hearings.

373/ DCRG Hearings, Tr. 395.

be no change in the competitive relationship among the different classes of stores. And if prices were lowered, then there would be a net benefit because the decreased revenue to the manufacturer would be passed on to the consuming public.

As for the second necessary condition, if the favored purchasers do pass their price savings on to their customers, it is unlikely that the result will be the elimination of significant number of the firm's competitors; at least not enough to increase its oligopoly power. As noted, small and large businesses most often do not perform the same function and are thus not engaged in full "head-to-head competition." Large firms may not regard the potential for price competition from small firms offering greater convenience as being significant enough to affect their own pricing practices. Thus, a major chain indicated that it considered most local independent food stores as capable of only "soft" competition and did not consider the presence of small firms in deciding whether to enter a given market. What really concerned the chain was the existence of other local or regional chains in the vicinity, because it was they, not the smaller businesses, which the national chain felt could actually engage in "hard" competition. 374/

Similarly, a Review Group witness representing independent tire dealers stated that after an extended period of alleged discriminatory pricing to one retail tire establishment, a businessman was forced to close two of his tire stores in an area, but that as far as he knew there were still several other competing tire stores in the area. 375/ No

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374/ National Tea Co., 69 F.T.C. 226, 321 (1966).

375/ Testimony of Philip Friedlander, DCRG Hearings, Tr. 429-30.

specific examples of instances in which secondary line discrimination so depleted the number of competitors in an industry that oligopoly power was significantly increased were presented to the Review Group. Given the very limited nature of Robinson-Patman protection, and the dynamic nature of the channels of distribution, it is unlikely that such instances exist to any important degree. Indeed, one attorney who testified before the House Small Business Committee in favor of Robinson-Patman, and who felt that the elimination of Robinson-Patman would, indeed, reduce the number of small businesses, nevertheless stated that competition among the firms remaining in a given market would be "vigorous." 376/

The head of the FTC's Bureau of Economics, in discussing the appropriate policy for enforcing Robinson-Patman stated his skepticism about the procompetitive effects of many proposed cases: 377/

> Specifically, is the goal in assessing competitive effects to maximize the vigor of competition, or to maximize the number of competitors who survive in the market? Through their training, most economists come to believe that society benefits when the vigor of competition is sustained over the long run. A further widely held tenet is that there is a positive correlation between the vigor or workability of competition and the number of competitors active in the market.
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> Still, it is also evident that maintaining vigorous competition in the short run might conflict with long-run vigor. Competition in the short run could conceivably be so intense that many viable, efficient competitors are driven from the market --

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376/ Prepared statement of Jerrold C. Van Cise, Subcommittee Hearings, pt. 2 at 222.

377/ Prepared statement of F. M. Scherer, Subcommittee Hearings, pt. 2. at 149.

so many indeed that the resulting market structure contains too few firms for competition to continue being vigorous. On the other hand -- and herein lies a crucial value judgment -- most economists believe that long-run viability of competition is not enhanced by preserving or protecting individual competitors whose operations are inefficient and whose costs therefore are so high that they continue to exist only at the sufferance of the industry's more efficient members. Economists are particularly inclined to favor the vigor of competition over the preservation of such high-cost competitors when economies of scale are sufficiently non-compelling and/or the entry of new efficient competitors is sufficiently easy that monopolistic pricing power is unlikely to emerge, even if some relatively inefficient competitors are forced to exit from the market.

Such judgments are difficult to make. The facts are often obscure, and how one comes out in a particular complex factual situation is likely to be influenced by how sanguine one is about the likelihood that vigorous competition will in fact survive the exit of competitors. A typical economist's study of numerous industrial histories is apt to induce somewhat more optimism on such matters than that which the drafters of the Robinson-Patman Act (and indeed, in those crisis-ridden times, the nation at large) manifested. This plus the economist's natural instinct to encourage market efficiency often leads to skepticism about the desirability of certain Robinson-Patman actions.

The third necessary condition is also unlikely to occur. No persuasive evidence was presented to the Review Group to demonstrate that if smaller enterprises were to leave a particular marketplace, prices would rise to a level higher than they would have been absent the granting of a discriminatory price to a particular retailer. The only specific allegation of this type of behavior is presented by the representative of the National Tire Dealers and Retreaders Association. He referred to an incident in which an outlet had, for two years, charged a retail price for its tires which was equivalent, it was claimed, to the wholesale price which competing independent businessmen paid for a similar tire. The witness went on, "Finally, our member closed two of his stores and the competing dealer then raised his prices by 40 percent to 50 percent. The consumer does not benefit in these price discrimination cases." 378/

According to data later supplied by the Association, however, the "gross profit on sales," that is, selling price minus cost of goods purchased, ranges from an average of 41.5 percent for those firms with 1974 sales under $750,000 to approximately 35.8 percent for those having over that figure. 379/ This gross margin translates into an average markup of 69 percent for the smaller firms, and 56 percent for the larger firms. Raising prices 40 to 50 percent over the usual retailers' purchase price from the manufacturer would merely reflect the resumption of the charging of the standard markup. In other words, consumers benefited from lower prices for two years, and thereafter merely resumed paying a price equivalent to the average retailers' markup over the manufacturer's price. As noted above, in this specific incident, many retailers remained in the market following the demise of the two mentioned outlets, and there is no reason to suppose that the vigor of competition over tire prices was any less.

Finally, the fourth necessary condition fails. No evidence was presented to the Review Group to show that if the smaller retailers in

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378/ Testimony of Philip Friedlander, DCRG Hearings, Tr. 388.

379/ Letter of Philip Friedlander to Donald Flexner, December 11, 1975.

a particular market were to exit because of price discrimination, the remaining merchants would have a free hand in raising prices above their previous levels. An increase in prices above the previous levels would lead to higher profits and thus make that particular market highly attractive to new entry. If prices rose above their previous levels, smaller merchants would prosper even if they had to pay discriminatorily high prices for the goods they purchased. Indeed, in one recent case decided by the Federal Trade Commission, a profitable smaller independent supermarket owner sold out to a larger national chain. The sale agreement included a restriction on the independent's reentering the supermarket business in that area for five years. Immediately at the expiration of those five years, the independent started up anew and prospered. 380/

If the remaining smaller businesses in the market believe that the larger operators are making windfall profits as a result of buying advantages, they would have a great incentive to form purchasing coops to reap the same advantages, thus renewing competitive vigor in the market. What evidence there is appears to support this proposition. In the late 1920s and early 1930s, A&P did not pass along to its customers all the savings it gained from its superior purchasing power and efficiency. It took some time for both the market to adjust to A&P's way of doing business and for A&P to adjust its prices downward to meet its lower costs. But by the time Robinson-Patman was enacted, A&P's financial success was already under challenge: 381/

380/ National Tea Co., 69 F.T.C. 226, 253-55, 264 (1966) (initial decision).

381/ F. M. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE, 251-52 (1970).

But A&P's very success created incentives for others to imitate its methods and introduce their own innovations (such as the supermarket). As they did, A&P's volume declined, dragging profits along. By 'pursuing a policy of making too much money,' A&P 'was slowly drowning in its own good fortune.' This slow-acting competition forced A&P to reassess its business policies, and one result was a concerted effort to reduce retail prices and price-cost margins. Ultimately, then, consumers were the beneficiaries of A&P's power as a buyer, but not without substantial delays. (Footnote omitted)

Today, however, delays need not be characteristic of the market response. Mr. Louis Fox, of Associated Wholesale Grocers, testified that should profits in any one area get too high, other enterprises would seek to enter: 382/

Mr. Flexner: Suppose in a retail market the profit margin started to edge up and became too high. What would be the result?

Mr. Fox: We have a real estate department. And we are looking for situations like this. And this is repeated all over the country. We have a real estate department that covers the area that we cover, looking at towns and cities where the gross margin may be too high. Take an example of a small town in the country where you have only one store, and the prices that he charges are exorbitant. We look at that town, we analyze the town, and we say, this is a town that we are going into to put in a supermarket. And then we go in there with a lower cost of operation and lower the food costs in that town. It is not only done in small towns, but is done in large cities by large chains. For example, I believe Safeway Stores went into the Houston market. They started doing the Houston market. Carl Fazio, who had -- I forget the name of his chain. He was out of Cleveland, who went into the Chicago market. Then he went to the Los Angeles market. So all over the

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382/ DCRG Hearings, Tr. 113-15.

country you have people in the food business that are looking for the situations where food costs are too high and they feel that they can go in there with a lower cost type of operation, or if they are making too much profit out of a market they will go in there and that is the type of market they look for, and they can go in there and get a good share of the market.

So I think history kind of shows that when a person gets too much of a share of a market that he always has competition moving in on him from other cities.

Mr. Flexner: Then you are saying that entry is fairly easy in retail grocery business?

Mr. Fox: No question about it. History proves that.

Similarly, in other markets, large firms, as well as small firms, may enter new markets or new industries where the incumbents are not operating efficiently, or are making high profit margins. Commenting on the fact that many larger enterprises are branching into forms of retail business other than those with which they had traditionally been associated, one study concluded: 383/

> The number of corporations with a newfound willingness to go anywhere and do anything in distribution will have increasing competitive impact. This development is likely to enlarge markedly concentration ratios at all levels of distribution.

In sum, the claim by proponents of Robinson-Patman that the increased occurrence of price discrimination that could be expected without Robinson-Patman would lead to reduced consumer welfare in the long run

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383/ Davidson, *supra* note 299, at 425.

is not supportable. There is no evidence that price discrimination does lead to, or should be expected to lead to, such levels of concentration as would give rise to oligopoly pricing on the retail side. Rather, the evidence shows that ease of entry in distribution is sufficient to make it highly unlikely that a retailer could for long maintain price levels above that generally characteristic of the industry.

d. Robinson-Patman Enforcement Has Not Aided Competition

There is also no evidence that Robinson-Patman enforcement orders have had positive effect on competition and prices in the markets in which they were entered. A pilot study of eight Robinson-Patman enforcement orders prepared by Professor Robert Brooks of Vanderbilt University for the FTC does not demonstrate that such orders resulted in any meaningful benefit to the consuming public. Professor Brooks, himself, concluded in testimony before the House Small Business Committee that most of the orders he studied seemed to have had little effect, good or bad, on "competition" in those industries. In at least one industry, though, he found that there indeed had been a positive benefit. 384/

Analysis of the Brooks report by the Trade Commission staff and by staff at the Department of Justice concluded that the Brooks report really does not offer much evidence of an improvement in competition resulting from the Robinson-Patman order studied. Indeed, it appears that Robinson-

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384/ Subcommittee Hearings, pt. 1 at 423. The Brooks Report is reproduced at Subcommittee Hearings, pt. 1 at 278. For a critique of the Brooks Report, see Wolfe, Reform or Repeal of the Robinson-Patman Act--Another View, 21 ANTITRUST BULL. 237 (1976).

Patman orders were often directed at markets which were already competitive, and the orders could do nothing to increase or decrease competition in those markets. The only effect of the orders seemed to be to increase the number of certain middlemen by reducing the ability of firms to grant discounts to their competitors. Specifically, an evaluation of the report by the Antitrust Division's Economic Policy Office found it difficult to find support in the Brooks Report survey responses for the conclusions Brooks drew. For instance, in four of the eight markets studied, Brooks concluded that: competition was already very effective, it was unlikely that Robinson-Patman Act enforcement could make it more effective, but if anything Robinson-Patman had had a positive effect. Yet there were the survey responses such as the following in one of these four industries:

> (an auto glass shop proprietor) 'Seems to feel that the order actually prevented competition in that it compelled the same benefits for everyone, whether they were trying to do a better job or not, which, in effect would be to discourage better dealers.'

In addition, Brooks concluded that for three industries studied (dairy, produce, and biscuits) Robinson-Patman enforcement did not improve a situation of inadequate competition, although it did have some good effects. Enforcement also had some bad effects, judging from the survey responses. In the final industry (office furniture) Brooks stated that Robinson-Patman had clearly caused improved competition.

It is difficult, however, to support Brooks' conclusion of an increased degree of price competition. In response to the survey question, "What are the differences in vigor of competitive rivalry in price from what you would have expected without the FTC ruling?", five respondents said that there had been no effect on price rivalry while only three said that price competition improved.

It seems entirely possible that the other benefits Brooks alleged (entry of new forms of competition, high degree of competition by middlemen) were due to the FTC order eliminating discounts to designers (buying direct) and thus creating a favorable climate for middlemen. One would naturally expect new middlemen to enter under this condition and, since discounts are made more rigid by the order, other forms of competition to arise. Clearly competition is different after the order and in a sense "new." It seems unlikely, however, that the modes of competition (service aspects, etc.) are as efficient after the order as before.

The report's conclusion that there was increased efficiency had support in the response to the survey question, "Have there been any changes in efficiency of sellers or buyers? (and what would have been expected without the order)." Four of the eight respondents stated that the market was less efficient after the order, due principally to increased use of middlemen dealers and less direct buying by designers. Two respondents noticed no effect of the order on efficiency. Only two respondents claimed the order increased efficiency. Significantly, one of these firms claiming an increase in efficiency was a dealer itself and the other was a manufacturer selling through an established network of dealers. Their replies to this question may reflect their self-benefit from the order.

Another study by FTC staff evaluated the effect of Robinson-Patman cease-and-desist orders on industry structure. 385/ The study concluded that issuance of a Robinson-Patman order had no significant effect on the ultimate structure of the industry involved. The authors, attorneys in the Compliance Division, noted that before a decision to enforce a previously issued order may be made, the Commission must consider whether the violation of an order is de minimis, examine and critique the various cost justifications included in reports of compliance, and finally, determine whether the costs of proceeding to enforce the order are outweighed by the benefits. Furthermore, it was noted that since the Commission, out of considerations of equity, does not file a civil suit until the respondent has been notified of defective compliance, a firm under order is encouraged to "try out" various schemes for legally evading the intent of the order. The authors believed that rule making and guidelines, often suggested as an alternative to the problem-ridden cease-and-desist order, would be ineffective unless the guidelines were so clear and the penalties so stiff as to completely deter attempts at avoidance. The Robinson-Patman Act, though, cannot be so forthrightly interpreted.

Without attempting to decide whether price differentials are uniformly bad as a matter of public policy, the FTC study concluded that where those

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385/ Field and Banta, An Evaluation of the Effects of Orders Issued Under the Robinson-Patman Act, printed in Hearings Before the Special Subcommittee on Small Business and the Robinson-Patman Act, 91st Cong., 2d Sess., Vol. 2 at 769 (1970).

discriminations which are arguably anticompetitive do occur, the structure of the industry itself is so inherently anticompetitive that antitrust enforcement would be better directed toward detection and prevention of merger, monopolization, and predation.

In short, the Field and Banta study contradicted a central assumption underlying the Robinson-Patman Act: that the enforcing agency, through its cease-and-desist orders, is able to prevent those practices which, if left unregulated, would in the long run lead to substantial concentration detrimental to the public interest. The study concluded: 386/

> (1) That there is no satisfactory evidence that price discrimination is significantly related to the general phenomenon of concentration in American industries; (2) that there is no persuasive evidence that the Commission's enforcement of the Robinson-Patman Price Discrimination Act has had any significant effect on either the structure, conduct or performance of any important American industry; . . .

e. Protection of Small Business Can Be Accomplished by Pro-Competitive Alternatives

i. Actual Predatory Pricing Can Be Prosecuted Under the Sherman Act

Empirical evidence, discussed in Section A, shows that below marginal-cost pricing rarely occurs. And no matter how likely such predatory practices may be on the manufacturing level, predatory pricing on the retail level is almost out of the question, due to the ease of entry in that sector. 387/ As this Report concluded, the only type of pricing which threatens potential harm

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386/ *Id.* at 769.

387/ Testimony of William F. Baxter, DCRG Hearings, Tr. at 58.

to competition is pricing below the incremental cost of supplying a particular commodity. It is precisely this type of conduct against which the Sherman Act is directed. 388/ Indeed, recent Appeals' Court cases dealing with Robinson-Patman have adopted the marginal cost test as the appropriate one for even Robinson-Patman analysis. 389/

Below-cost predatory pricing, to the extent that it does occur, would arise logically only where the predator believed that the expected costs of predation would be made up at a later time because of the firm's ability to charge high monopoly prices. The presence of substantial firms in the industry, or ease of entry would likely deter even the most enthusiastic predator, since either condition would deny the predator monopoly profits. Only where a firm attempts to monopolize a market, alone or in a conspiracy with others, or is involved with other firms in a concerted effort to eliminate or discipline competitors by predatorily low pricing, is the likelihood of success sufficient to encourage predation. But it is of course precisely when the firm attempts to monopolize the market, conspires to do so, actually does so, or enters into an agreement with other firms in the industry to fix prices -- at any level -- that the firm violates Sections 1 and 2 of the Sherman Act. These offenses, following recent Congressional revision, are now felonies, punishable by three years in prison, and up to a $1 million fine for each participating

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388/ See Areeda & Turner, Predatory Pricing and Related Activities Under Section 2 of the Sherman Act, 88 HARV. L. REV. 697, 701-03 (1975).

389/ International Air Industries v. American Excelsior Co., 517 F.2d 714 (5th Cir. 1975), *cert. denied.*, 44 U.S.L.W. 3488 (1976).

company, sanctions which are in addition to liability for treble damages. Exposure to these extremely harsh penalties must of course be weighed along with simple cost factors by the aspiring predator.

Antitrust enforcement experience suggests that predatory pricing in an oligopolistic industry would likely involve an intra-industry conspiracy. The United States recently convicted several members of the Gypsum industry of just such conspiratorial predation, a conviction which is now under appeal. The chief prosecutor in the Antitrust Division's case against the Gypsum industry case agreed that "as far as predatory aspects are concerned, the Sherman Act is well equipped to deal with the type of predation" which was alleged in the Gypsum case: the actual attempt by competing manufacturers to eliminate the competition of small producers or to restrict that competition to regional markets. He also testified that it would be unlikely that any one of the few large companies that make up an oligopolistic industry would engage in a predatory pricing campaign without some sort of agreement from its major competitors. 390/

Perhaps the clearest evidence of the ability of the Sherman Act to deal with the predatory practices at which Robinson-Patman was directed is the conviction of A&P for conspiring to restrain trade in, and to monopolize, the grocery industry, and the aceptance of no contest pleas from

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390/ Testimony of John Fricano, DCRG Hearings, Tr. 67-68.

other chains for similar violations. 391/ The conviction in the 1946 A&P case was based on more than price discrimination. Also included were several allegations relating to buying practices and market manipulations. The trial judge in his decision finding A&P guilty of having violated the Sherman Act, offered a telling criticism of Robinson-Patman 392/

> Sometimes I doubt whether we ever needed Robinson-Patman with all its elusive uncertainty. I have thought that the Sherman Act properly interpreted would have remedied all the ills meant to be cured. . . . This plan, this mechanism did not break down; it has never needed more than proper execution and enforcement. Too often, I fear, we enact a new law to cure mal-administration of an old one. So Congress enacted the Robinson-Patman Act. I doubt if any judge would assert that he knows exactly what does or does not amount to violation of the Robinson-Patman Act in any and all instances. Mr. Chief Justice Hughes exclaimed to the Federal Bar Association in 1931: "How difficult it is to secure legislation that is simple and unequivocal."

Thus, former Assistant Attorneys General for Antitrust Donald Turner and Thomas Kauper agree that the Sherman Act provides adequate protection against any real predatory activity. 393/ Professor Turner stated before the Review Group that those who insist on the necessity of Robinson-Patman to prevent primary line discrimination really want to prevent not predation, but increased competition: 394/

391/ United States v. New York Great A&P Tea Co., 67 F. Supp. 626 (E.D. Ill. 1946), aff'd, 173 F.2d 79 (7th Cir. 1949); United States v. Safeway Stores, Inc., Cr. 7196, D. Kansas (plea entered 1948); United States v. Kroger, Inc., Cr. 7197 D. Kansas (plea entered 1948). Additionally, consent decrees have been entered to enjoin certain uses of loss leaders and geographic discrimination undertaken with anticompetitive effect or intent. United States v. Safeway Stores, Inc., 1957 CCH TRADE CASES ¶68,871 (E.D. Tex. 1957) (consent decree).

392/ 67 F. Supp. at 676-77.

393/ Testimony of Donald F. Turner, DCRG Hearings, Tr. 305; Testimony of Thomas E. Kauper, Id., at 343.

394/ DCRG Hearings, Tr. 315-16.

The problem, the real problem -- and the people who want to keep the Robinson-Patman Act know what they are doing -- is that they confidently assume -- and the past cases will back them up -- that the interpretation of law under the Robinson-Patman Act will be far more prohibitory than a reasonable prohibition of predatory pricing under the Sherman Act, and they want that. They want a law which makes it extremely difficult for a seller to move out of his territory and absorb some of the savings in transportation costs in order to compete in a distant market. They don't want that. They want to stop a seller from cutting a price on certain business, thereby taking away from other competitors. In other words, . . . there are people that would like to see the Robinson-Patman Act kept because they don't like price competition, and they feel that the Act as it is presently written and as it is presently interpreted will indeed put some constraints on what, by an economic test, is legitimate competition that a sensible interpretation of the Sherman Act would not prohibit.

So, I would say that if you are only dealing with the question of the Robinson-Patman Act as it applied to competition among sellers, that this Act could and should be repealed as being at best redundant and at worst a very serious and anticompetitive piece of legislation.

ii. Small Businessmen Can Form Cooperative Organizations to Counter Large Firm Buying Power

The success of many retailer buying cooperatives points up a crucial fact: Of all the factors favoring large enterprises, the factor that small businessmen can most easily counteract is that of quantity and other discounts which can be achieved through larger scale buying. This was known when the Act was passed, as the 1935 FTC Report pointed out: 395/

395/ 1935 CHAIN STORE REPORT 56.

Data procured by the Commission indicate that in the grocery trade an appreciable proportion of the buying advantages of the chains can be overcome by fairly large and well-organized cooperatives.

A 1966 FTC study 396/ of the food industry indicated that cooperatives and voluntary associations have their primary impact in the areas of group buying and warehousing, and somewhat less success in the area of cooperative advertising.

An example of the success of the cooperative in equalizing buying power was given by Mr. Fox, President of Associated Wholesale Grocers. He testified that his cooperative successfully equalized the purchasing power between the independent and the chains. In fact, a large national chain had become a member of his coop because the chain could obtain supplies more cheaply from the coop than it could on its own. The cooperative, with a volume of more than $550 million annually, could use its buying power and efficiency for the benefit of all members. 397/

Mr. Fox gave a concrete example of how a small businessman, through partnership with a coop, can outperform a chain store: 398/

> We had an A&P store that closed down. And our company negotiated to purchase the store at book value, which meant the fixtures were low on

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396/ 1966 FTC FOOD STUDY, supra note 105, at 286.

397/ Testimony of Louis Fox, DCRG Hearings, Tr. 108.

398/ Id. at 104-06.

the books. And this particular store was doing about $12,000 a week and was a losing proposition for A&P.

We had a small retailer who had a store doing about $4,000 a week in a deteriorating neighborhood that we knew would be out of business within three or four years. But he was aggressive and he had his family that he wanted to put, that was in the store with him, but not enough volume to readily keep him in business.

We placed the store in his hands. We helped to finance him. We took the lease and subleased it to him. This man went into the store and he increased the volume by doubling the amount to about $20,000 a week. I was curious to find out why he was able to double the amount of volume that A&P did. I went into the store and I found the owner in the front. And he was a goodwill man, more or less, greeting customers.

He asked me to go around the store. He introduced me to all of his help. He introduced me to his son, Don, who was the head of the meat department, greeting the customers, giving them what they wanted. His son, Tom, was head of produce; he took care of the produce department. His daughter was one of the checkers, in charge of the checkers. His wife was in the office taking care of the phone calls and bookkeeping. He was up front.

And I happened to listen to a consumer that came up to him at the time. And she said, you know, since you have taken over the store, it is much brighter, much cheerier, and I seem to feel at home here as if you value my business.

There is no question that you can't beat that. So all he needed was the opportunity. That store today is doing double the amount of what he was doing at that time. So he continues to grow. And sooner or later he will go to store number two. This is what we do to help retailers.

4. Conclusion

Robinson-Patman is ineffective when evaluated both in terms of its narrow, protectionist objectives, and in terms of its benefits to the welfare of society as a whole. The greater the business community's compliance with Robinson-Patman, whether as a result of voluntary action or vigorous public or private enforcement, the greater the Act's deleterious impact upon competition. However, and this is the anomaly inherent in the law, it cannot be said that an increase in compliance produces a corresponding increase in protection for small business. For, as the preceding analysis shows, Robinson-Patman is largely irrelevant to the survival, success or failure of the small business class in the long run. Rather, the forces of consumer choice and the market remain determinative of success and failure. At the same time the Act has not shown itself to be capable of promoting the antitrust goals of continued competitive vigor and low prices. In fact, the Act is regulatory in nature and its enforcement is based on a series of faulty presumptions. The other antitrust laws are capable of protecting against genuine predation, and the ingenuity of those small businessmen who are agressive and competent will ensure the maintenance of a strong small business sector.

Having explored the effects of Robinson-Patman, the arguments of its proponents, and the economic and business realities which underlie its effectiveness, this Report will now turn to its ultimate conclusions about the Act.

Chapter V. CONCLUSIONS

A. Robinson-Patman Has Survived Because it Appeals to Basic American Beliefs of Equality and Fairness

The Robinson-Patman Act became law at a time in American history of great economic uncertainty and concern that the free enterprise system had been a failure. The nation had just experimented with the NRA's Codes of Fair Competition, an experiment in non-competition in American society. The previous decades had seen the birth and growth of the large American corporation. To many it was an alien way of economic life and cause of fear for American small business. Perhaps the spirit of the times can best be exemplified in this quote from a partial concurrence of Justice Benjamin Cardozo in a Supreme Court decision upholding the Florida chain store tax: 399/

> There is a widespread belief that the existing unemployment is the result, in large part, of the gross inequality in the distribution of wealth and income which giant corporations have fostered; that by the control which the few have exerted through giant corporations, individual initiative and effort are being paralyzed, creative power impaired and human happiness lessened; that the true prosperity of our past came not from big business, but through the courage, the energy and the resourcefulness of small men; that only by releasing from corporate control the faculties of the unknown many, only by reopening to them the opportunities for leadership, can confidence in our future be restored and the existing misery be overcome; and that only through participation by the many in the responsibilities and determinations of business, can Americans secure the moral and intellectual development which is essential to the maintenance of liberty. If the citizens of Florida share that belief, I know of nothing in the Federal Constitution which precludes the State from endeavoring to give it effect and prevent domination in intrastate commerce by subjecting corporate chains to discriminatory license fees. To that extent, the citizens of each State are still masters of their destiny.

399/ Louis K. Liggett Co. v. Lee, 288 U.S. 517, 580 (1933).

It was in this spirit of the times that Congress, and the legislatures of the several states, looked with favor upon several proposals which would protect the independent small businessman and his way of doing business from the economic power of the larger enterprise -- and its efficiencies, new ways of distributing products, and better entrepreneurial skill. The legislative response to this "big business challenge" was basically three fold: chain store taxes, fair-trade laws, and Robinson-Patman.

Chain store taxes soon were repealed or grew into disuse because they were blatantly directly at one group of businesses regardless of a particular chain's way of doing business or ability to serve the public. Fair-trade laws, although only recently eliminated from the national scene, were long looked upon with disfavor by most because they permitted explicit price-fixing agreements. These agreements denied the consuming public the freedom to choose between high-price, high-service retail establishments and those that offered only a lower price but not much in the way of convenience or assistance. Robinson-Patman is no different in purpose than chain-store taxes and resale price maintenance. With respect to chain-store taxes, the Federal Trade Commission in 1935 clearly stated that the protectionist aspects of the statute would not only be contrary to the principles of our free enterprise system, but would be injurious to large segments of the public as well. 400/

> To tax out of existence the advantages of chain stores over competitors is to tax out of existence the advantages which the consuming public have found in patronizing them, with a consequent addition to the cost of living for that section of the public. That portion of the public which is able to pay cash and is willing to forego delivery service in return for the advantage of lower prices will be deprived of that privilege, generally speaking, although there are exceptions both ways. It will also tend toward an arbitrary frustration of whatever saving in cost of production and distribution results from integration of the functions of producer, wholesaler, and retailer. So on the whole the number of people adversely affected by such a tax would constitute a very substantial percentage in comparison with the number adversely affected by present conditions. The graduated tax on chain stores cannot accomplish fully the social ends aimed at by such legislation without producing incidentally these results.

Similarly, the Congressional Report on legislation designed to repeal resale price maintenance legislation rejected the notion that such legislation should be used for the purpose of protecting small retailers from competition: 401/

> [T]o the extent that the "Mom and Pop" retailer charges a higher price because he is providing more services to his customer, consumers should have the freedom to choose between paying more for those services and buying nothing but the unadorned product at a lower price from a competitor. And testimony before the Subcommittee indicated that many consumers are in fact willing to pay a somewhat higher price for the convenience, courtesy and service which small retailers are uniquely situated to provide.

400/ 1935 FTC CHAIN STORE REPORT 91-92.

401/ H. REP. No. 94-341, 94th Cong., 1st Sess., at 4 (1975).

Robinson-Patman, on the other hand, has remained with us. The reason for this is that its basic protectionism is concealed: the Act is one of the antitrust laws, and is claimed to rest on the principle of "equality of opportunity." Indeed, the evidence before the Review Group shows that the presence of Robinson-Patman does serve in spirit to make more concrete the concept of fairness in business dealings. The Act may also serve to give businessmen a psychological boost in their struggle to remain competitive with other enterprises in their market, and to provide a degree of bargaining strength in negotiations with their suppliers. Unfortunately, Robinson-Patman, so just in principle, cannot be supported as a net benefit to American society because its real effects as an economic regulatory statute are on balance more costly than beneficial to society.

B. The Basic Goals of Robinson-Patman Cannot Be Achieved <u>By Statute; But The Law Imposes Great Costs on Society</u>

The simple truth is that Robinson-Patman is a false promise: it provides little, long-run protection to small businessmen. It is just not possible to legislate equality in a free market system. The basic force in changing the structure of the American marketplace is the consumer. It is the consumer who decides the type of retail establishment with which he or she wishes to deal. The consumer makes the choice as to whether he or she wishes the personalized service and convenience of a small establishment, providing special goods with special know-how, or the lower prices, relatively less service, and greater inconvenience of a larger store. This Report has shown that in the highly dynamic distribution sector, there are many reasons why some businessmen fail and others succeed. New types of establishments arise, populations shift in age and location, and changes in the overall economic picture may make the public more or less willing to pay for the ambience of a service-oriented establishment. Also, new products are developed, new methods of distribution come into play, and businessmen serving once useful functions find they are no longer needed. In this environment, it is highly deceptive -- even futile -- to rely on a law prohibiting non-cost justified price differences for commodities of like grade and quality, as a device for insuring equality of competitive opportunity.

The author of a voluminous study of the impact of Robinson-Patman also concluded that the goal of guaranteeing small businesses a mythical "equality of opportunity" as opposed to that of preserving competition in the marketplace was both an inappropriate aim of a price discrimination statute and impossible to achieve through the mechanism of prohibiting certain price discriminations: 402/

> To the present writer it appears that, even in the of the powerful buyer, the objective of preserving equal opportunity is an inappropriate focus for a law of price discrimination. The pursuit of equality through the price discrimination law, even in this limited field tends to give the law an unfortunately pervasive control over price relationships. Moreover, the definition of equality as the equivalent of equal buying prices distorts the concept of equal opportunity. A powerful buyer may obtain advantages not only by paying lower prices but also by receiving more generous credit, obtaining quicker deliveries, obtaining preferential access to scarce goods,

402/ EDWARDS, supra note 107 , at 641.

> and in many other ways. Piecemeal legislation addressed to particular types of advantage is not a satisfactory way of assuring equality, if, indeed, equality is to be assured by law. To keep public control over business activity within reasonable limits and at the same time to cope more effectively with the greatest disparities of bargaining power, the focus of public policy should be shifted from efforts to control market behavior to efforts to prevent undue concentrations of power. Section 2 of the Clayton Act [Robinson-Patman] cannot fill the need created by underuse of Section 7 of the Clayton Act and Section 2 of the Sherman Act.

In return for this illusory "protection" the small businessman, and American business in general, is placed under a series of legal restrictions and administrative agency rules and guidelines that can genuinely be described a "regulatory." Moreover, the evidence also indicates that for several reasons, it is the small businessman, not the large businessman who runs afoul of Robinson-Patman and must bear the expense of litigation with the Federal Government.

Perhaps, though, the protectionist heritage of Robinson-Patman and its unsuitability to the task of protecting the small businessman might be overlooked if the statute did promote and preserve competition in the marketplace and there were no less anticompetitive alternatives such as enforcement of the Sherman Act. Of course, public policy is deeply concerned by increases in market concentration. The reason for this is simple. There is a belief that in many markets increased concentration means increased pricing inflexibility, price fixing, and the erection of barriers to entry which forestall new competitors and thus eventually lead to the decline of innovation in the protected, incumbent industries.

The perversity of Robinson-Patman is that it achieves for many sectors of the American economy precisely those ill effects of concentration about which the American public is rightly concerned. As has been stated, Robinson-Patman really serves as "fair trade" at the manufacturer level. By promoting "pricing caution," Robinson-Patman encourages the maintenance of uniform list prices in oligopolistic manufacturing industries. At the same time, by discouraging bargaining on part of the buyers, Robinson-Patman decreases the possibility that a retailer will receive a lower price, pass it on to the consumer, and thus initiate a competitive struggle in the retailing sector which will ultimately result in more efficient operation and lower prices for the consumer. Robinson-Patman has served to encourage the notion that businessmen may talk about price, or indeed even fix prices, if the purpose of such activities is to increase compliance with the Robinson-Patman Act. Of course, businessmen who intend to fix prices will fix them, but it is certainly contrary to the public interest to retain on the books a law that encourages businessmen to take the fatal first step of discussing prices with competitors by seducing them with the notion that if they do engage in actual price fixing, Robinson-Patman may get them off the hook. Finally, by preventing promotional price cuts Robinson-Patman discourages entry into new markets and competition for new customers. Indeed, the evidence shows that Robinson-Patman may protect actual monopolies against new entry and cause the reduction of the number of competitors in a market by making litigation expenses prohibitive. Likewise, Robinson-Patman serves to hurt the small businessman when it prohibits suppliers from helping small retailers meet their competition from competitors' products when it cannot be positively shown whether the competing large retailer is simply lowering the price on its own, or is actually receiving a special allowance from its suppliers.

In return for the Robinson-Patman Act's fostering the effects of concentration in markets, little actual increase in competition can be attributed to the Act. Moreover the evidence available shows that there appears to be no significant effect on the number of small businesses due to Robinson-Patman, or because of the even more protective "fair trade" laws, although there are doubtless individual businessmen who would not be in existence today but for Robinson-Patman.

Perhaps, the most fitting contrast of small business attitudes towards Robinson-Patman with the actual effects on small businessmen of its repeal was given by one Rhode Island hardware dealer when surveyed about the effects on him of the end of that state's fair trade laws: 403/

> Although I had actively fought the repeal of the state's Fair Trade law, the actual repeal of the law had made no difference to my operations. The dire consequences of the repeal of Fair Trade, which I had predicted, did not materialize because of a substantial increase in retail business in the state. I feel that small retailers were not hurt by the repeal of the Fair Trade law and in no way wish to see Fair Trade back on the books

403/ A. HOURIHAN & J. MARKHAM, THE EFFECTS OF FAIR TRADE REPEAL: THE CASE OF RHODE ISLAND III-13, 14 (1974).

in Rhode Island. . . . I myself have joined a cooperative buying group and, by buying through this group direct from the manufacturers, am able to sell at lower prices while netting the same profit margin on sales. In conclusion, I feel that the only definite disadvantage of Fair Trade's demise in Rhode Island pertained to wholesalers and not to retailers or consumers. I frankly admit that I feel that I have been mistaken in devoting my time to fighting the repeal of the Fair Trade law, and that, in the last analysis, Fair Trade simply did not matter that much.

Of course, some value judgments do remain. There are those who believe that a statute which is intended to benefit the small businessman deserves support where the law does not appear to be in contradiction to the fundamentals of the marketplace. This Report, however, concludes that the narrow protectionist purpose of Robinson-Patman and its anticompetitive effect far outweigh the perceived benefits of the Act's existence for small businessmen. Moreover, the Report finds that Robinson-Patman provides relatively ineffective assistance to small business.

This Report has sought to contribute a deeper understanding of Robinson-Patman so that the public policy task of reconciling Robinson-Patman to the economic realities of present day America may be carried out. The Report's suggested remedies in this regard are set out in the next chapter.

Chapter VI. POSSIBLE REMEDIES

The evidence reviewed in this Report makes clear that careful reconsideration of the Robinson-Patman Act is timely. This evidence seriously undermines historic claims that the Robinson-Patman Act offers any sustaining economic protection to small business; and it raises serious questions whether the Act advances the competitive goals of other antitrust laws. Rather, the evidence is that the Act promotes high prices, restricted entry, and inefficiency in the distribution of goods; and it has encouraged the creation of illegal pricing exchanges by competing manufacturers. The fact that the Act does not apply at all to the offering of services -- a growing sector in which small business is especially significant -- reinforces the conclusion that the Robinson-Patman Act is not a key factor in preserving efficient small businesses. Rather, such businesses survive, in any field, largely on their ability to provide what the public wants: better service, greater convenience, and at times, lower prices.

The testimony of antitrust enforcement officials is that genuinely predatory activity that threatens small business can be prevented by the Sherman Act, but any prohibition directed against non-predatory price discriminations only subjects the business community to needlessly complex regulatory restrictions. Such restrictions are inherently more likely to impede procompetitive behavior than to prevent activity that may ultimately lead to lessened competition. Thus, serious consideration should be given to repealing the Robinson-Patman Act, and Section 2 of the Clayton Act which it amended.

Many believe that the Robinson-Patman Act's prohibitions against non-cost justified price discriminations are an important part of our antitrust laws. It was in recognition of this conviction that the Antitrust Division of the Department of Justice in the Summer of 1975 prepared and made available for comment two draft statutes dealing with pricing behavior. For the benefit of those who desire to draw upon the Justice Department statutes and the public reaction to these proposals in attempting to draft a better price discrimination law, this Report will briefly discuss those statutes and the comments which have been made about them.

The two Department of Justice draft statutes were the "Predatory Practices Act of 1975," which was directed toward predatory actions against one's own competitors, and the "Price Discrimination Act of 1975," which contained the provisions of the Predatory Practices Act and additionally outlawed certain price discriminations which might affect competition among the seller's customers. (The draft statutes are included in Appendix C.) As found in this study, enforcement of Robinson-Patman is based on the inference that certain types of price discrimination will lead to changes in market structure and the further inference that such changes are likely to have an adverse impact on competition in that market. The purpose of the Justice drafts was to forbid price discrimination only in cases where its practice would probably cause adverse market effects. Basically, the proposed Predatory Practices Act would outlaw the charging of a price below the "reasonably anticipated average direct operating expense" incurred in supplying a particular customer with a commodity for a sustained length of time, unless certain defenses based on lack of competitive harm were met. No discrimination need be proved. The Act also outlawed certain overt threats of harm made to a person's competitor in order to deter him from taking certain procompetitive actions. The proposed Price Discrimination Act, aside from incorporating the provisions of the first statute, in general would outlaw price discriminations which were either part of a pattern which "systematically favors larger recipients" in the market in which the disfavored purchaser is located, or which clearly threaten to eliminate from a market a competitor of a seller's customer where the elimination of such competitor may lessen competition in the marketplace. A discrimination may be defended by showing that it was based on a reasonable estimate of cost differences or in an attempt to meet competition.

Comments on the draft proposals were forthcoming both in the Domestic Council Review Group Hearings and in the hearings on the Robinson-Patman Act held by the Ad Hoc Subcommittee on Antitrust, the Robinson-Patman Act, and Related Matters of the House of Representatives Committee on Small Business. A synopsis of the comments in both forums is included as "Appendix D."

As can be seen from that discussion, it is very difficult to draft a statute which limits its coverage to those forms of pricing behavior which have great potential for anticompetitive harm but little potential for procompetitive benefit, and is at the same time administratively workable. Perhaps the most profound indication of the magnitude of this task was the statement by a former Federal Trade Commission staff member who in concluding a 700-page study of Robinson-Patman, remarked that the actual legislative language which "would determine the focus of the price discrimination law as applied to injuries in the secondary line . . . would need to be worked out with great care. The author is not equipped for this task and has not attempted it." 404/ For those endeavoring to undertake the task, however, three basic approaches are offered:

1. Reduce the ability of private parties to invoke legal process for the purpose of reducing the vigor of its rival's competition --

The setting of prices is perhaps the most delicate area of the competitive process. As one witness noted in Congressional testimony, the mere fact of a businessman's complaint is not sufficient to show competitive injury. 405/ Yet, Robinson-Patman permits a competitor to file a lawsuit in a great many circumstances merely upon the allegation that one of his competitors is charging or receiving a low price. Such a lawsuit threatens treble damage liability -- often awarded under an automatic damages rule -- extensive attorneys fees, and the burden of extensive discovery procedures which may reveal confidential pricing and cost data. Such a procedure may permit firms to effectively coerce either

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404/ EDWARDS, supra note 107, at 652.

405/ Testimony of Robert Brooks, Subcommittee Hearings, pt. 1 at 429.

competing buyers or sellers into adhering to uniform prices.

Due to the overriding need to weigh carefully both the potential benefit and the potential harm to competition from a given price reduction, it is essential that Robinson-Patman actions not be initiated without a serious attempt to evaluate the impact upon the public interest of a given enforcement action. Private parties cannot be reasonably expected to base their decisions to sue on public interest grounds; they necessarily will consider Robinson-Patman litigation as one more weapon to overcome competitive advantages. As shown the threat of private action can effectively deter price competition: prices will remain uniform, even when the seller honestly believes a price cut would be lawful. Consequently, an effective way of reducing the adverse effects of Robinson-Patman would be to eliminate the right of private action and leave Robinson-Patman enforcement to the Federal Trade Commission. If it is felt that at least some private remedy should be retained, the punitive element of treble damages could be removed and the damages for Robinson-Patman violations be limited to single damages, computed on the basis of actual damages suffered and without any recourse to a rule of automatic damages. Punitive damages are inappropriate where their effect would be to deter procompetitive behavior.

2. Make the defenses realistic --

A second approach to reducing the anticompetitive effect of Robinson-Patman would be to make the cost-justification and meeting competition defenses more in accord with actual business practice. As the evidence presented to the Review Group has shown, a businessman has no way of really knowing at the time he is making a pricing decision whether a discount will prove to be cost justified in the eyes of the Federal Trade Commission or the courts: his accounting practices may ultimately prove unacceptable or the businessman may simply not be able to assemble all the relevant data down to the last penny at the time he is making his decision. Moreover, insofar as the actual sale price is dependent on the cost of production or delivery some time in the future, in today's inflationary economy the businessman may not have any way of knowing the actual cost structure of his business at the time delivery is made. Consequently, businessmen must be permitted to make reasonable, good faith estimates of the costs involved in a particular transaction, and to make estimates of the cost differences of serving particular groups which are based on reasonable business practice.

While some judicial decisions have substantially improved the operation of the meeting competition defense, a revised Robinson-Patman should make clear that a businessman may use the defense "offensively" to gain new customers as well as to retain old customers, and he should also be able to utilize any pricing system or classification which is reasonably and in good faith designed to enable himself or his customers to counteract the marketing strategy of the competitor. Similarly, revisions should be made to insure that a businessman will not be held liable for meeting the unlawful price of one of his competitors, unless that other competitor is also called to account for his illegal pricing behavior.

3. <u>The offenses prohibited by Robinson-Patman should be made more realistic</u> --

The most fundamental change that can be made in Robinson-Patman is to redefine the affirmative case required to establish a prima facie violation of Robinson-Patman more in accord with the economics of the marketplace. Here, two approaches are possible. First, price discrimination can be redefined to mean non-cost justified discrimination, thus making it the plaintiff's burden to establish the discrimination's unreasonable relationships to costs as well as its mere existence. This change would conform the gravamen of the action with the theoretical antitrust justification for a price discrimination statute.

Under the Federal Rules of Civil Procedure, broad discovery of information under the control of the defendant is permitted. Since cost data would be material to the plaintiff's case, such information would be discoverable. A defendant's failure to produce data is subject to several sanctions including a finding that the evidence would have been in favor of the plaintiff. 406/ The United States and private parties have litigated many cases under the antitrust laws in which the plaintiff had to prove a pricing practice based upon information held by the defendant.

While such a shift in burdens would make the proving of an affirmative case more difficult -- in case of doubt as to whether or not the cost justification existed, the plaintiff would fail -- such

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406/ FED. R. CIV. P. 37(b)(2)(A).

a result is appropriate. If the available facts are laid on the table, and doubt remains, the businessman who sought to lower his price should prevail, rather than a competitor who claims that a lower price is not in the public interest.

Second, those seeking to reform Robinson-Patman might also wish to consider narrowing those situations in which courts may presume competitive injury. The Act is currently interpreted by many courts to prohibit, on the primary line, pricing below the fully allocated cost of doing business in a given market, and on the secondary line, non-systematic price discrimination which affects the resale price of a commodity. Yet, the evidence shows that it is fallacious to infer on evidence of such behavior alone a likelihood of ultimate injury to competition in a significant number of cases. Thus, those interested in making serious reforms in Robinson-Patman should attempt to limit the definition of predatory pricing and/or harmful price discriminations to situations which are highly likely to harm competition. In this regard, predatory pricing should be determined by the variable costs, not the fully allocated costs of the alleged predator; and harmful discrimination should be found only where there is systematic favoritism of large purchasers over small.

4. Eliminate the per se provisions of Sections 2(c), (d), and (e) --

The regulatory content of Robinson-Patman could be significantly reduced by elimination of the per se provisions of the Act dealing with brokerage and promotional allowances and facilities. The brokerage provision, based on experience with A&P's brokerage operations in the 1920s and 30s, and on a desire to protect independent brokers, can safely be repealed. Any legitimate concern over the use of brokerage payments as a form of indirect price discrimination can be dealt with by making clear that brokerage payments should be netted against price for the purpose of determining the existence of a discrimination under Section 2(a).

Such a folding of Section 2(d) and (e) into the general prohibitions on discrimination is more difficult. Promotional payments or the granting of facilities or services may be made independently of any particular sale of merchandise. Consequently, it may be difficult to net such transactions against the cost of goods to determine the existence of discriminatory sales. If a statute covering allowances is to be retained, then, it might well be made a separate provision of Robinson-Patman. A violation of this revised statute should depend on a showing of competitive harm, and defenses based on meeting competition and cost justification should explicitly be made applicable. Consideration should also be given to including a provision which would permit the seller to show that a difference in allowances was reasonably related to the expected return to the seller of granting the allowance.

The interdependence of the first recommendation, limiting the availability of private action, and the next two, redefining the Act's scope and defenses, is apparent. Limitation of Robinson-Patman violations to price discriminations which are systematic and to predatory pricing which is below variable costs will sharply reduce the ability of the private plaintiff to interfere with legitimate pricing competition. Since such activities properly defined may produce harm to competitors as well as competition some remedy should be made available to those injured by such behavior. Consequently, the greater the narrowing of the statute's coverage, the stronger becomes the case for maintaining some form of private damage action. Conversely, if it is felt that the Act's coverage should remain broad, then the scope of private remedies must be decreased in order to reduce the current ability of private plaintiffs to engage in litigation intended to eliminate legitimately competitive pricing behavior.

The need today is for pragmatism in dealing with the burdens which the Robinson-Patman Act has imposed on the competitive process. This Report represents our best effort to achieve this result and to formulate responsive remedies.

Appendix A: PROJECT STAFF

The Report was prepared in the Department of Justice during the tenures of Assistant Attorneys General Thomas E. Kauper and Donald I. Baker by Antitrust Division attorneys Richard O. Levine and A. Theodore Gardiner III, under the immediate supervision of Donald L. Flexner, Acting Chief of the Division's Regulated Industries Section and the overall guidance of Jonathan C. Rose, Deputy Assistant Attorney General. Also contributing to the preparation and analysis of the Report were Robert W. Wilson and Bruce R. Snapp, economists in the Division's Economic Policy Office whose Director is George Hay.

Appendix B: THE ROBINSON-PATMAN ACT

Section 2

(a) It shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly, to discriminate in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, and where the effect of such discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them: Provided, That nothing herein contained shall prevent differentials which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered: Provided, however, That the Federal Trade Commission may, after due investigation and hearing to all interested parties, fix and establish quantity limits, and revise the same as it finds necessary, as to particular commodities or classes of commodities, where it finds that available purchasers in greater quantities are so few as to render differentials on account thereof unjustly discriminatory or promotive of monopoly in any line of commerce; and the foregoing shall then not be construed to permit differentials based on differences in quantities greater than those so fixed and established: And provided further, that nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade: And provided further, That nothing herein contained shall prevent price changes from time to time where in response to changing conditions affecting the market for or the marketability of the goods concerned, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned.

(b) Upon proof being made, at any hearing on a complaint under this section, that there has been discrimination in price or services or facilities furnished, the burden of rebutting the prima-facie case thus made by showing justification shall be upon the person charged with a violation of this section, and unless justification shall be affirmatively shown, the Commission is authorized to issue an order terminating the discrimination: Provided, however, That nothing herein contained shall prevent a seller rebutting the prima-facie case thus made by showing that his lower price or the furnishing of services or facilities to any purchaser or purchasers was made in good faith to meet an equally low price of a competitor, or the services or facilities furnished by a competitor.

(c) It shall be unlawful for any person engaged in commerce, in the course of such commerce, to pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other party to such transaction or to an agent, representative, or other intermediary therein where such intermediary is acting in fact for or in behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid.

(d) It shall be unlawful for any person engaged in commerce to pay or contract for the payment of anything of value to or for the benefit of a customer of such person in the course of such commerce as compensation or in consideration for any services or facilities furnished by or through such customer in connection with the processing, handling, sale, or offering for sale of any products or commodities manufactured, sold, or offered for sale by such person, unless such payment or consideration is available on proportionally equal terms to all other customers competing in the distribution of such products or commodities.

(e) It shall be unlawful for any person to discriminate in favor of one purchaser against another purchaser or purchasers of a commodity bought for resale, with or without processing, by contracting to furnish or furnishing, or by contributing to the furnishing of, any services or facilities connected with the processing, handling, sale, or offering for sale of such commodity so purchased upon terms not accorded to all purchasers on proportionally equal terms.

(f) It shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section.

Section 2a

It shall be unlawful for any person engaged in commerce, in the course of such commerce, to be a party to, or assist in, any transaction of sale, or contract to sell, which discriminates to his knowledge against competitors of the purchaser, in that, any discount, rebate, allowance, or advertising service charge is granted to the purchaser over and above any discount, rebate, allowance, or advertising service charge available at the time of such transaction to said competitors in respect of a sale of goods of like grade, quality, and quantity; to sell, or contract to sell, goods in any part of the United States at prices lower than those exacted by said person elsewhere in the United States for the purpose of destroying competition, or eliminating a competitor in such part of the United States; or, to sell, or contract to sell, goods at unreasonably low prices for the purpose of destroying competition or eliminating a competitor.

Any person violating any of the provisions of this section shall, upon conviction thereof, be fined not more than $5,000 or imprisoned not more than one year, or both.

Appendix C: THE 1975 DEPARTMENT OF JUSTICE DRAFT REFORM PROPOSALS

The proposed modifications of the Robinson-Patman Act took the form of two alternative statutes. The first, "The Predatory Practices Act of 1975," outlaws sustained selling at a price below the seller's average current direct operating expense, an accounting approximation of short run marginal cost, unless the seller has a small market share or is meeting competition. The proposed statute also outlaws overt threats to coerce businessmen to charge noncompetitive prices or refrain from or cease serving specific customers or geographic areas. These provisions are relatively objective standards designed to prevent actions that would not normally be undertaken without an anticompetitive purpose while permitting low prices which may often be part of procompetitive promotional or entry efforts. In so doing, the legislation applies to situations of primary line predation not involving price discrimination.

The alternative statute, "The Price Discrimination Act of 1975," incorporates the provisions of the Predatory Practices Act and additionally makes unlawful certain types of secondary line price discrimination which are not cost-justified. The prohibited discriminations are those which are a part of a pattern which systematically favors large firms over their smaller competitors and those which clearly threaten to eliminate a competitor who, under a Clayton Act test, is significant with respect to the maintenance of competition in the particular market. Additionally, the statute makes more flexible the cost and meeting competition defenses currently in the Robinson-Patman Act, and extends the coverage of that Act to include attempted discriminations. The proposed secondary line sections are thus designed to limit coverage of the Act to discriminations which serve no real competitive need, but which potentially are harmful to small business (systematic favoritism to large buyers), and those which actually threaten to eliminate a competitively necessary rival.

PREDATORY PRACTICES ACT

Be it enacted, etc., that this Act shall be known as "The Predatory Practices Act of 1975."

Sec. 2. It shall be unlawful for the seller of a commodity engaged in commerce overtly to threaten a competing or potential competing seller of the commodity with economic or physical harm, so as to cause or induce the competing seller (a) to conform to pricing policies favored by the seller; or (b) to cease or refrain from selling any commodity to any particular customer; regardless or whether any overt action is taken to fulfill such threat.

Sec. 3. It shall be unlawful for a seller of a commodity, engaged in commerce, knowingly to sell on a sustained basis such commodity at a price below the reasonably anticipated average direct operating expense incurred in supplying the commodity, where such commodity is sold for use, consumption, or resale within the United States, the District of Columbia, or any other territory under the jurisdiction of the United States.

Sec. 4. It shall be a defense to a violation of Section 3 that an otherwise unlawful price:

(a) was charged by a person in order to meet in good faith an equally low price of a competitor;

(b) was charged by a new entrant, a person having at the time of sale a less than 10 percent share of the sales of the commodity in the section of the country in which the commodity was sold at such price being deemed a new entrant;

(c) was charged in response to changing conditions affecting the market for or the marketability of the commodities involved, such as but not limited to actual or imminent deterioration of perishable commodities, obsolescence of seasonal commodities, distress sales under court process, or sales in good faith in discontinuance of business in the commodities concerned; or

(d) did not clearly threaten the elimination from a line of commerce of a competitor of the person charging the otherwise unlawful price.

Sec. 5. As used herein:

(a) "Commerce" shall have the same meaning as in Section 1 of the Act of October 15, 1914 (38 Stat. 730) commonly known as the Clayton Act;

(b) "Price" shall mean the exaction of all consideration diminished by the granting of any brokerage, advertising, promotional, or other allowance, or the furnishing of services or facilities;

(c) "Economic harm" shall include a reduction of revenues by sales at a price below the direct operational expense incurred in supplying the commodity, destruction of goodwill, and the withdrawal of credit without cause from a person;

(d) "Physical harm" shall include (i) physical damage to or destruction of real property, plants, buildings, equipment or other physical assets of a business enterprise or of those individuals managing, operating, owning or controlling a business enterprise, and (ii) physical injury to or physical intimidation of individuals engaged in managing, operating, owning or controlling a business enterprise;

(e) "Direct operating expense" shall include only direct costs of production and distribution associated with the particular sales of the commodities in question and only the portion of costs of depreciation, capital, leases of land and productive facilities, and general overhead and advertising, the incurring of which vary directly with the quantity of commodity which is produced; and

(f) "to sell on a sustained basis" shall mean to sell the commodity in question for more than 60 days within a period of one year.

Sec. 6. Any person violating any of the provisions of this Act shall be guilty of a misdemeanor and upon conviction thereof, shall be fined not more than $100,000 or imprisoned for not more than one year, or both.

Sec. 7. This Act shall be considered one of the "antitrust laws" for the purposes of Section 1 of the Act of October 15, 1914 (38 Stat. 730). Provided, however, that this Act shall not be construed to limit the applicability of such antitrust laws.

Sec. 8. Section 5 of the Federal Trade Commission Act shall not be held to prohibit any discrimination in price for the sale of commodities, or the receipt of any such discrimination.

Sec. 9. Section 2 of the Act of October 15, 1914 (38 Stat. 730) commonly known as the Clayton Act, as amended, and Sections 1 and 3 of the Act of June 19, 1936 (49 Stat. 1528) commonly known as the

Robinson-Patman Act, are hereby repealed. Any orders or decrees entered pursuant to the sections enumerated in the proceeding sentence shall expire two years after the enactment of this Act, or sooner if they so provide.

Sec. 10. The Federal Trade Commission is hereby empowered to enforce the provisions of this Act as if they were provisions of the Act of October 15, 1914 (38 Stat. 730).

ROBINSON-PATMAN ACT REFORM STATUTE

(* denotes sections contained in Predatory Practices Act)

Be it enacted, etc., that this Act shall be known as "Price Discrimination Act of 1975."

*Sec. 2. It shall be unlawful for the seller of a commodity engaged in commerce to overtly threaten a competing or potential competing seller of the commodity with economic or physical harm, so as to cause or induce the competing seller (a) to conform to pricing policies favored by the seller or (b) to cease or refrain from selling any commodity within a geographic area or to cease or refrain from selling any commodity to any particular customer; regardless of whether any overt action is taken to fulfill such threat.

*Sec. 3. It shall be unlawful for a seller of a commodity, engaged in commerce, knowingly to sell on a sustained basis such commodity at a price below the reasonably anticipated average direct operating expense incurred in supplying the commodity, where such commodity is sold for use, consumption, or resale within the United States, the District of Columbia, or any other territory under the jurisdiction of the United States.

*Sec. 4. It shall be a defense to a violation of Section 3 that an otherwise unlawful price:

(a) was charged by a person in order to meet in good faith an equally low price of a competitor;

(b) was charged by a new entrant, a person having at the time of sale a less than 10 percent share of the sales of the commodity in the section of the country in which the commodity was sold at such price being deemed a new entrant;

(c) was charged in response to changing conditions affecting the market for or the marketability of the commodities involved, such as but not limited to actual or imminent deterioration of perishable commodities, obsolescence of seasonal commodities, distress sales under court process, or sales in good faith in discontinuance of business in the commodities concerned; or

(d) did not clearly threaten the elimination from a line of commerce of a competitor of the person charging the otherwise unlawful price.

Sec. 5. It shall be unlawful to discriminate either directly or indirectly in price between different purchasers of commodities of like grade and quality, where either or any of the purchases involved in such discrimination are in commerce, where such commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possesion or other place under the jurisdiction of the United States, where:

(a) the recipient of the discrimination is in competition with others not granted the discrimination, the discrimination is significant in amount, and the discrimination is part of a pattern which systematically favors larger recipients in the relevant line of commerce over their smaller competitors; or

(b) the recipient of the discrimination is in competition with others not granted the discrimination, the discrimination is significant in amount, and the discrimination clearly threatens to eliminate from a line of commerce one or more competitors of the recipient where the effect of such elimination may be substantially to lessen competition or to tend to create a monopoly in any line of commerce in any section of the country.

Sec. 6. It shall be a defense to a violation of Section 5 that the lesser price was charged in good faith to meet an equally low price of a competitor. Except in a suit seeking only prospective relief against all or substantially all of the competitors practicing the discrimination, the defense shall be allowed even if the equally low exaction of a competitor is subsequently determined to be unlawful.

Sec. 7. It shall be a defense to a violation of Section 5 that the lesser price makes an appropriate allowance for differences in the cost of manufacture, distribution, sale, or delivery resulting from the differing methods or quantities involved in supplying the customers in question. An allowance is appropriate where the difference in price does no more than approximate the difference in cost; where the difference in price does not exceed a reasonable estimate of the difference in cost; or where the estimated difference in cost is the result of a reasonable system of classifying transactions which is based on characteristics affecting cost of manufacture, distribution, sale or delivery, under which differences in price among classes approximate differences in cost.

Sec. 8. It shall be a defense to a violation of Section 5 that: (i) the lesser price was in response to changing conditions affecting the market for or the marketability of the commodities involved, such as but not limited to actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith in discontinuance of business in the goods concerned; or (ii) the lesser price was available, on reasonably practicable conditions, to the person allegedly discriminated against.

Sec. 9. Nothing herein contained shall prevent any person from refusing to deal with any person. An offer to deal only on discriminatory terms shall, however, be treated as a completed transaction for the purpose of according relief under this Act.

*Sec. 10. Section 5 of the Federal Trade Commission Act shall not be held to prohibit any discrimination in price for the sale of commodities, or the receipt of any such discrimination.

Sec. 11. An order or injunction issued to restrain or prohibit a violation of Sections 5 through 9 shall remain in effect for a limited time, stipulated at the time of entry, and reasonably related to the nature of the violation. In no case shall an order issued to enforce such sections remain in effect more than five years after the date of entry.

*Sec. 12. Section 2 of the Act of October 15, 1914 (38 Stat. 730) commonly known as the Clayton Act, as amended, and Sections 1 and 3 of the Act of June 19, 1936 (49 Stat. 1528) commonly known as the

Robinson-Patman Act, are hereby repealed. Any orders or decrees entered pursuant to the sections enumerated in the proceeding sentence shall expire two years after the enactment of this Act, or sooner if they so provide.

*Sec. 13. As used herein:

(a) "Commerce" shall have the same meaning as in Section 1 of the Act of October 15, 1914 (38 Stat. 730) commonly known as the Clayton Act;

(b) "Price" shall mean the exaction of all consideration diminished by the granting of any brokerage, advertising, promotional, or other allowance, or the furnishing of services or facilities;

(c) "Economic harm" shall include a reduction of revenue by sales at a price below the direct operating expense incurred in supplying the commodity, destruction of goodwill, or the withdrawal of credit without cause from a person;

(d) "Physical harm" shall include (i) physical damage to or destruction of real property, plants, buildings, equipment or other physical assets of a business enterprise or of those individuals managing, operating, owning or controlling a business enterprise, and (ii) physical injury to or physical intimidation of individuals engaged in managing, operating, owning or controlling a business enterprise;

(e) "Direct operating expense" shall include only direct costs of production and distribution associated with the particular sales of the commodities in question and only the portion of costs of depreciation, capital, leases of land and productive facilities, and general overhead and advertising, the incurring of which vary directly with the quantity of the commodity which is produced; and

(f) "to sell on a sustained basis" shall mean to sell the commodity in question for more than 60 days within a period of one year.

*Sec. 14. This Act shall be considered one of the "antitrust laws" for the purposes of Section 1 of the Act of October 15, 1914 (38 Stat. 730). Provided however, that this Act shall not be construed to limit the applicability of such antitrust laws.

*Sec. 15. Any person violating Sections 2 or 3 of this Act shall be guilty of a misdemeanor and upon conviction thereof, shall be fined not more than $100,000 or imprisoned for not more than one year, or both.

*Sec. 16. The Federal Trade Commission is hereby empowered to enforce the provisions of this Act as if they were provisions of the Act of October 15, 1914 (38 Stat. 730).

A. Section-by-Section Analysis of the Predatory Practices Act of 1975

Section 2 makes it unlawful for a seller of a commodity engaged in commerce to threaten overtly one or more of his competitors with "physical" or "economic" harm (both terms are defined in Section 5) so as to cause or induce the competitor to conform to pricing policies favored by the threatening seller or to cease or refrain from selling a commodity to a particular customer or within a particular geographic area. The Section is intended to promote competitive pricing by making unlawful the communication of overt threats (not mere signals that may be inferred from price behavior) to cause losses of income (arising from below average direct operating expense prices), credit, property or property values, or to cause physical injury so as to induce a competitor to follow a noncompetitive pricing strategy in spite of his desire to act competitively. Similarly, the section would outlaw efforts to use coercion to induce a competitor or potential competitor to cease serving a particular market or customer.

By outlawing communications about a firm's intention to engage in predatory conduct, the ability of a firm to control market behavior through threats rather than by sustained price cutting is obviously reduced. This prohibition, coupled with a reduction in predator credibility brought about by the Act's provisions dealing with sustained below cost pricing, reduces the likelihood that businesses would initially make the judgment that a predatory pricing campaign would be profitable in the long run.

Section 3, in conjunction with the defenses provided in Section 4, is intended to make unlawful prices which have a genuinely predatory potential, while permitting pricing policies that may be part of legitimate efforts to enhance competition through new entry or other promotional efforts. The section makes illegal the knowing charging of prices for a commodity on a sustained basis (defined by Section 5 as greater than 60 days) which are below the seller's reasonably anticipated average direct operating expense (also defined in Section 5), a level which is meant to approximate the economists' definition of short-run marginal cost. This is fundamentally a prophylactic rule and does not require the showing of anticompetitive intent.

Section 4 establishes four defenses to Section 3. The first permits a seller to match a price charged by a competitor. The presence of this defense, however, is not intended to remove liability for a violation of Section 2 of the Sherman Act if a business goes below its average variable cost in meeting competition as part of an attempted monopolization. The good faith requirement would prevent several firms which were parties to the same strategy of intimidation from relying on each others' below-cost prices as a defense, though such a concerted effort would most likely also be a violation of Section 1 of the Sherman Act.

The second Section 4 defense excludes from the prohibitions of Section 3 by a new entrant. A firm which had a less than 10 percent share of the relevant market at the time the contested price was charged is deemed a new entrant. This defense serves two purposes. The first is to allow promotional pricing by new entrants into the industry. The second is to make clear that the Act is not concerned with below-cost pricing by a firm whose market share is so small that its pricing activities could not reasonably be viewed as likely to confer undue market power. Regardless of the initial size of the firm, as soon as it achieved a 10 percent market share, the firm would bear the burden of showing it was a new entrant.

The third defense under Section 4 permits distressed sales of obsolete or deteriorating commodities, sales under court process, or in the course of going out of business. This defense, based on that contained in the current Robinson-Patman Act, excludes from the Act's coverage below-cost sales which are not part of an on-going course of dealing, but merely are a part of an effort to obtain the salvage value of the goods in question.

The last defense permits a showing that an otherwise unlawful price did not clearly threaten the elimination of a competitor of the firm charging the low price. The defense thus precludes a finding of liability where the charging of a below direct operating expense price does not result in serious harm either to competition or a competitor. This provision is intended to permit, for example, the use of loss leaders and the like by retailers.

Section 5 sets out the definitions for the Act:

"Commerce" is defined as in the Clayton Act and is limited to the movement of commodities in interstate commerce, not merely movements which affect interstate commerce. This standard incorporates the narrow definitions contained in Gulf Oil Corp. v. Copp Paving Co., 419 U.S. 186 (1974).

"Price" is defined in a comprehensive manner to include all consideration exacted as part of the sale, diminished by any allowances, services, or facilities provided by the seller.

"Economic harm" includes a reduction of revenues resulting from the charging of prices below the average direct operating expense of supplying the commodity, destruction of goodwill, and the unjustified withdrawal of credit. A decrease by a seller of his prices, designed to force a matching reduction by his competitor in order to cause a loss of income would thus be included in this definition only if the seller's price were below his average direct operating expenses.

"Physical harm" is described in a comprehensive manner and includes the destruction of real property, equipment, etc., of the competitor and also that belonging to those who own or manage the business. Similarly, physical intimidation of those in the management group is included.

"Current direct operating expense" is defined to include only those variable costs directly incurred in supplying the commodity in question and to exclude that portion of fixed costs, such as accounting depreciation, debt service, rentals, etc., which are not dependent on the amount of the commodity provided. The intent is to approximate the economists' definition of short-run marginal cost, but in a way that is simpler for businessmen and accountants to determine. See Areeda & Turner, supra, at 716.

"To sell on a sustained basis" is established as a period of 60 days, a time designed to permit promotional pricing by firms having a greater than 10 percent share of the market and to permit some flexibility with respect to the time interval used by firms to recalculate their costs.

Section 6 makes violation of the provisions of the Act a misdemeanor punishable by $100,000 fine and/or a year's imprisonment. Section 7 makes the Act one of the "antitrust laws," thus providing for treble damage and injunctive relief.

Section 8 removes from the Federal Trade Commission the power to utilize Section 5 of the FTC Act against price discrimination.

Section 9 repeals the operative provisions of the Robinson-Patman Act, and Section 2 of the Clayton Act, which contains provisions of the Robinson-Patman Act.

Section 8 removes from the Federal Trade Commission the power to utilize Section 5 of the FTC Act against price discrimination.

Section 9 repeals the operative provisions of the Robinson-Patman Act, and Section 2 of the Clayton Act, which contains provisions of the Robinson-Patman Act.

Section 10 empowers the Federal Trade Commission to enforce the Act in the manner it now enforces the Clayton Act.

B. Section-by-Section Analysis of the "Price Discrimination Act of 1975"

The Price Discrimination Act of 1975 is compatible with the proposed Predatory Practices and deals more comprehensively with pricing actions which have strong anticompetitive potential. Sections 2, 3, and 4 of the Price Discrimination Act are identical to the similarly numbered provisions of the Predatory Practices Act discussed above, and are likewise meant to prevent predation between a seller and his competitors by means of below average current direct operating expense pricing and/or by overt threats.

Section 5 in conjunction with the defenses set out in Sections 6 through 8 modifies the current Robinson-Patman standards regulating price discrimination so as to make unlawful only those discriminations on the secondary level, i.e., between favored and disfavored customers of the seller, which have the most potential for harm to the competitive process. The prohibited discriminations are of two types. The first is a discrimination which is part of a pattern which systematically favors larger recipients in the relevant market over their smaller competitors (The Morton Salt test). Excluded from the coverage of this provision would be occasional discounts or those given to a few of several similarly situated firms. Thus the fact that a large firm had received a price concession would not trigger the Act. Only if it could be shown that a seller routinely gave non-cost justified discounts to a class of larger sellers and that such discounts did not become part of a subsequent reduction passed on to most buyers, would the seller be brought under this section. The second prohibited discrimination is a cost differential of such a nature that it clearly threatens to eliminate from the relevant line of commerce or market one or more competitively significant rivals. The standard used to gauge competitive importance is that contained in Section 7 of the Clayton Act, i.e., the effect of the elimination of the competitor "may be substantially to lessen competition or tend to create a monopoly."

Section 6 continues the current meeting competition defense contained in the Robinson-Patman Act and makes explicit the recent trend in judicial decisions under that Act which permits the defense to be made in spite of the illegality of the price being met. The only exception to the latter rule would be that the defense could not be offered in an injunctive action against unlawful pricing.

Section 7 expands the current cost justification provisions and permits the defendant to justify a discrimination where the amount of the discrimination does no more than approximate the difference in the cost of supplying the commodity between the buyers, or a reasonable estimate thereof, or is based on a reasonable system of classifying purchasers.

Section 8 continues the current defense based on changing market conditions for the goods, distress sales, and sales in discontinuance of business. Also made explicit is the judicially recognized defense that the lesser price was available on reasonably practicable conditions to the person allegedly discriminated against.

Section 9 continues the current proviso that this Act does not operate to compel parties to deal with one another. The section, though, does change current law by providing that an offer to sell at discriminatory terms, though rejected by the buyer, shall be considered a "sale" for purposes of establishing jurisdiction.

Section 10 recognizes that this statute is intended to establish the federal law with respect to price discrimination and thus prevents Section 5 of the Federal Trade Commission Act from independently being used to regulate the granting or receipt of any discrimination in price.

Section 11 requires that the duration of any order or injunction issued to restrain violations of Sections 5 through 9 of the Act that deal with price discrimination as opposed to predatory pricing or the use of threats, shall be reasonably related to the nature of the violation and in no case shall be more than five years.

Section 12 repeals the operative portions of the Robinson-Patman Act and Section 2 of the Clayton Act which has been amended to contain the Robinson-Patman Act's major provisions. Orders or injunctions under the sections would expire in two years unless they provide for an earlier date.

Section 13 contains the definitions for the Act, which are identical to those in the "Predatory Practices Act of 1975."

Section 14 denominates the Act as one of the "antitrust laws" as defined in Section 1 of the Clayton Act, thus making the injunctive and treble damage remedies of the Clayton Act applicable, and provides that the Act should not be construed to affect the applicability of the antitrust laws.

Section 15 makes the violation of Sections 2 or 3, dealing with threats and predatory pricing, misdemeanors punishable by a fine of up to $100,000 and/or imprisonment of up to one year.

Section 16 empowers the Federal Trade Commission to enforce the Act.

The proposed Act thus eliminates the absolute prohibitions on brokerage and other allowances contained in the present sections 2(c), (d), and (e). Discriminations involving such allowances would be covered by the main provisions of the statute since "price" is defined to take such allowances into consideration. Buyer liability is also eliminated.

Appendix D: RESPONSE TO DEPARTMENT OF JUSTICE DRAFT REFORM PROPOSALS

On July 9, 1975, the Antitrust Division of the Department of Justice released a paper, "Reform of the Robinson-Patman Act", discussing problems created by the Act and suggesting certain possible reforms. While not making formal recommendations for legislative change, the paper did contain two draft proposals, "The Predatory Practices Act of 1975" and "The Price Discrimination Act of 1975", which seemed logical responses to the problem areas highlighted in the study of the statute.

The proposals were circulated for the purpose of eliciting comment on their provisions and on the general problem of price discrimination. Response to the Robinson-Patman preliminary study and the draft proposals has spurred a renewed debate over the Robinson-Patman Act's effect upon the way in which prices are set in a changing economy.

In its January 5, 1976, letter requesting the testimony of Federal Trade Commission members and staff, the Ad Hoc Subcommittee on Antitrust, The Robinson-Patman Act, and Related Matters requested each witness to speak to:

> Your views concerning the suggested repeal of the Robinson-Patman Act and some reach of Section 5 of the Federal Trade Commission Act suggested substitution therefore as evidenced by the enclosed copies of the so-called "Robinson-Patman Act Reform Statute" and the so-called "Predatory Practices Act of 1975." The record of this Ad Hoc Subcommittee shows that these suggested measures were proposed by certain members of the staff of the Department of Justice Antitrust Division. In addition, your views concerning the impact of such suggested legislation upon the body of the antitrust laws in the event such suggested bills should be enacted into law.

In addition, The Domestic Council Review Group Hearings on the Robinson-Patman Act heard testimony from interested persons concerning the draft proposals. This section will catalog the suggestions and comments on the proposals presented during the two proceedings.

A. Substantive Objections

Most witnesses opposing the draft objected that thev would leave unregulated pricing behavior which presently would be unlawful under the statute, and, to that extent, the proposals represented a repeal of the Robinson-Patman Act. The most common objection was that, with respect to primary line effects, both proposals, unlike the present statute, would reach only "sustained" sales below "reasonably anticipated average direct" costs. Witnesses argued that the effect of allowing sales at or above direct costs would be to allow destructive predatory pricing: 407/

> It is my opinion that a seller could engage in behavior having recognized anticompetitive consequences without coming within the ambit of the proposed legislation. As a matter of fact, I doubt whether very many of the decided cases in which primary line injury has been found would have been brought under either of the proposed laws.

If such behavior were legalized, some witnesses argued, large firms would, through predatory pricing, drive their smaller rivals from the marketplace: 408/

> The proposed new legislation is defective, in the first place, because it repeals the 1914 prohibition of price discrimination where this trade practice is engaged in by large sellers with the probable effect of substantially lessening the competition of small sellers. Once more powerful companies would be free under this new proposal to sell commodities in the markets of local competitors at "below cost or without a fair profit" while raising their prices "above their fair market value" in other markets.

407/ Prepared Statement of Paul R. Dixon, Subcommittee Hearings, pt. 3 at 83.

408/ Prepared Statement of Jerrold G. Van Cise, Subcommittee Hearings, pt. 2 at 221-22.

By eliminating only "sustained" below cost sales, defined as sales below cost for more than 60 days within a one year period, the opponents argued that the proposals miss a great deal of predation. For example, it was pointed out that a favored customer could stock a year's supply of goods within a 60 day period. 409/ Another Commission witness pointed out that a great deal, including the demise of a business, could take place in 60 days. 410/

In a similar vein, those opposing the reform proposals argued that the definition of below cost, "below the reasonably anticipated average direct operating expense incurred in supplying the commodity" is less protective than the present statute. Commissioner Hanford questioned whether the precise definition in the drafts might not hamper the FTC's ability to respond flexibly in the face of diverse predatory pricing situations: 411/

> The specific proposals you have asked me to review are troublesome in several respects. I have, for example, reservations about the wisdom of adopting a predatory pricing standard which would lock us into a rigid definition, such as a "price below the reasonably anticipated average direct operating expense" incurred in supplying the commodity. I am particularly concerned that inflexible statutory criteria may impede our ability to respond to the needs of dynamic markets. Predatory pricing strategies, as a practical matter, are not necessarily geared to precise accounting definitions of cost; nor should the analytical framework of antitrust be so confined. In some situations we may find that a pricing strategy for sales slightly above a firm's "anticipated average direct operating expenses" over a long period of time can have adverse competitive consequences. Sometimes an effective strategy, designed to block the growth

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409/ Testimony of Ernest G. Barnes, Subcommittee Hearings, pt. 2 at 172.

410/ Testimony of Eugene A. Higgins, Subcommittee Hearings, pt 2 at 176.

411/ Prepared Statement of M. Elizabeth Hanford, Subcommittee Hearings, pt. 3 at 78-79.

or expansion of a firm's competitors, may follow a pattern of pricing which falls below the proposed statutory definition for brief periods of time, then rises slightly, and falls again if competition threatens to make in-roads on the predator's market. The antitrust laws must, in my judgment, remain sufficiently flexible to deal with pricing strategies of this type, particularly in instances in which it appears entry into highly concentrated markets is being deterred.

Commissioner Nye, on the other hand, expressed general agreement with the definition of below cost pricing, but questioned the need for legislative revision since the federal courts, prompted by leading antitrust experts, may be moving in the direction of the Department of Justice approach. 412/

> The second thrust of the draft of the "Predatory Practices Act" appears to be an attempt to codify the concepts espoused by Professors Areeda and Turner in their recent article in the Harvard Law Review. I admit to being in tentative agreement with these scholars, but their principal point is that the conduct they describe is already illegal under Section 2 of the Sherman Act. I believe it can probably also often be reached under Section 2(a) of the Clayton Act, Section 5 of the Federal Trade Commission Act and Section 3 of the Robinson-Patman Act as well. Thus, with eyes newly opened, sustained pricing below average variable cost may now be challenged by the Justice Department, the Federal Trade Commission and the private bar. As I noted earlier, at least one appellate court has adopted the theory. Until such time as it appears that Professors Areeda and Turner are wrong as to the present state of the law, we should let their views guide judicial development, rather than rushing to codify those views (with Volume 88 of the Harvard Law Review providing the authoritative legislative reference).

Many responses to the drafts expressed concern with the Reform Statute's decreased application, and the Predatory Practices Act's total lack of protection, in the secondary line situation. 413/ The

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412/ Prepared statement of Stephen Nye, Subcommittee Hearings, pt. 3 at 102. (footnotes omitted).

413/ Prepared statement of Paul R. Dixon, Subcommittee Hearings, pt. 3 at 84.

draft Reform Statute would make it unlawful to discriminate in price between different purchasers of commodities of like grade and quality, where the discrimination is significant in amount and systematically favors large over small purchasers, or where the discrimination clearly threatens to eliminate a competitor, tending to lessen competition or create a monopoly. In both cases, the proscribed effect must be to threaten those in competition with the firm receiving the discriminatorily favorable price.

First, opponents of the proposal pointed out that the draft, by limiting its protection to those in competition with the favored customer, would prevent application of the proposal to third or fourth line injury situations: 414/

> For example, Section 5 of the proposed Reform Statute would prohibit "significant" price discrimination which is "part of a pattern which systematically favors larger recipients over their smaller competitors." This provision would apparently limit relief to the secondary level (i.e., direct customers of the discriminatory sellers), and would not permit customers further down the distribution chain to recover against the original supplier. I believe that this modification of the present law would be undesirable. And I reference the Perkins v. Standard Oil case, 395 U.S. 642 (1969), which I argued in the U.S. Supreme Court, and where the Ninth Circuit was reversed. Standard was alleged to have passed on discrimination through not the customer of the customer, the third line, but the customer of the customer of the customer. The Court said you can't do this; this is evasion. And no matter how far down the line you pass on discrimination, if it injures competition, it can be challenged under the Robinson-Patman Act.

414/ Testimony of Earl W. Kintner, DCRG Hearings Tr. 167-68. See also Kintner, Reform of the Robinson-Patman Act: A Second Look, 21, ANTITRUST BULL. 203 (1976).

Second, some objected to the proposal's approach of prohibiting only systematic discrimination favoring large over small purchasers. The objections to this provision were summarized by Commissioner Nye: 415/

> The draft of the so-called "Robinson-Patman Reform Statute" consists in part in a new exposition of existing law, which I find undesirable for reasons noted earlier, and in part in the erection of additional requirements for the successful prosecution of a price discrimination action. Section 5(a) establishes a cause of action requiring that an illegal discrimination be "part of a pattern which systematically favors larger recipients". I have two questions: First, how long will it be before clever businessmen--likewarship commanders evading submarines--learn to devise intricate and seemingly random courses of action in order to frustrate the showing of a systematic pattern? And does it really matter much to the disfavored buyer--large or small--that he had to buy at prices higher than those paid by both larger and smaller competitors? I believe not. Second, as Mr. Kauper's Special Assistant, Joe Sims, made clear to another Subcommittee of the Small Business Committee last July 10, the favored buyer is not necessarily the biggest buyer. The draft assumes, incorrectly, that he always is, or at least that he must be for the disfavored customer to obtain relief.

One FTC staff member objected to any decrease in secondary line protection, maintaining that protection at the secondary, tertiary, and further levels is necessary to prevent concentration at one level, say the manufacturing level, from trickling down, causing concentration at other stages of distribution. 416/

> . . . I believe the danger of serious competitive erosion at the distributor and retailer levels of competition is a matter of real and continuing competitive concern. This is particularly true where oligopolistic supply markets are involved. Competitive erosion is fostered by systematic discriminationsin price and hidden promotional

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415/ Prepared Statement of Stephen Nye, Subcommittee Hearings, pt 3 at 102.

416/ Testimony of Bartley T. Garvey, Subcommittee Hearings, pt. 2 at 165.

> and advertising subsidies, which aid and abet the gradual transference of the industry concentration that exists at the producer level downward to customer levels. The laws seeking to retard this process can, perhaps, be improved, but, in my view, should certainly not be weakened or diminished.

Both reform proposals were criticized for expanding the defenses available to one charged with pricing behavior presently governed by the Robinson-Patman Act. Both reform drafts allow, as a defense to predatory pricing charges, proof that the below cost price was used by a new entrant to penetrate a new geographical market. By defining "new entrant" as a firm with less than a 10 percent market share, however, it was argued that the reform proposals would allow predatory market penetration by large national concerns able to subsidize losses from profits reaped elsewhere: 417/

> This would be an open invitation to any large national concern to move in and force an independent that did not have resources in other areas of the country out of business. Ten percent of a market is not a bad share and even if an independent had a 20 percent share, [his loss of 10 percent could possibly eliminate him as a viable competitor.] When a national concern attempts to move into an area, where there is a local competitor and one or two nationals, it is the local competitor who is knocked out. Large national concerns can use reserves from other areas to meet the low prices of a new entrant until the independent sells out or goes bankrupt, at which time prices usually go up.
>
> The Supreme Court upheld a predatory pricing case against Continental Baking Co. where its market share increased from 1.3 to 8 percent of the market. It may also be noted that illegal mergers often involve less than a 10 percent market share.

In dealing with either a charge of predatory pricing or price discrimination, the draft proposals would judge the legality of a

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417/ Prepared statement of Eugene A. Higgins, Subcommittee Hearings, pt. 2 at 177. (footnotes omitted).

price on the basis of approximate rather than exact costs. With respect to price discrimination, one witness maintained that allowing a cost defense on the basis of reasonable approximations "would effectively emasculate the proposed statute." 418/ And to define predatory pricing as pricing below "reasonably anticipated" direct costs would be, it was argued, to provide no protection at all. 419/

> This, of course, would operate to allow predatory market invasions by sellers, including those with monopoly resources available from any number of other markets, to sell at unreasonably low prices, which would be carefully anticipated to be just a trifle above the statutorily defined cost level, even when such a market invasion might demonstrably seriously injure competition in the invaded market and eliminate even the most efficient of smaller, local, or regional producers.

A further criticism of the two proposals' treatment of costs was that the predatory pricing provisions placed on the complaining party the burden of proving that the prices charged were below costs. 420/

> Section 3 also has a built-in enforcement problem since it would require the agency to prove the seller's cost. One of the chief criticisms of the Robinson-Patman Act has been that the defense of cost justification imposes too great a burden on the seller by requiring it to prove its own costs. Under the new proposals, the burden would be on the agency to prove that the seller was selling below its direct operating expenses. This would be difficult enough if the seller manufactured and sold only one commodity. For a multi-product company or for a company producing joint products with common costs such as oil and gasoline, the burden would be formidable indeed. In any event, I think such a burden is best placed on the party most able to shoulder it, namely the seller itself.

418/ Testimony of Ernest G. Barnes, Subcommittee Hearings, pt. 2 at 173.

419/ Testimony of Bartley T. Garvey, Subcommittee Hearings, pt. 2 at 164.

420/ Prepared statement of Paul R. Dixon, Subcommittee Hearings, pt. 3 at 84.

A number of witnesses expressed concern that the draft proposals altered the present statute's incipiency standard for determining impact upon competition. The Robinson-Patman Act allows the inference that a price discrimination, if large enough to affect resale prices, will cause injury to a specific firm. And if such injury is inferred, the Act presumes that injury to competition has occurred.

The reform proposals require a showing that the behavior in question presents a substantial risk that competition will be adversely affected. Under the predatory pricing provisions, the defense that the act did not threaten the elimination of a competitor is allowed; price discrimination would be unlawful only if it consistently favored large over small purchasers or threatened to eliminate competitors where the effect of such elimination is a tendency toward monopoly or a reduction in competition.

Commissioner Hanford felt that such a standard might offer too little protection in secondary line cases. 421/

> While it may be argued that unsystematic discrimination may have, in many cases, no impact or a "trivial" adverse impact on competition, the option to proceed, if substantial injury should occur, should not be foreclosed. The alternative Section 5(b) would afford protection only in instances in which the discrimination, although unsystematic, "clearly threatened" to eliminate a competitor. In the latter situation, unfavored customers which are not necessarily on the border line of becoming a failing company may, as a result of discrimination, be less able to compete effectively or may fear retaliation if they do compete; but there could be no recourse.

421/ Prepared statement of M. Elizabeth Hanford, Subcommittee Hearings, pt. 3 at 79.

Another Commission witness had a similar objection to the primary line provisions: 422/

> A further requirement to establish a violation of the proposed statute would be a showing that the discrimination would clearly threaten the elimination of a competitor from a line of commerce. This language would place a heavy burden on the party attempting to prove a violation. In my opinion, this language would require substantial economic evidence and proof of a direct causal relation between the discrimination and the demise of a competitor. This burden of proof is in sharp contrast to the existing proof of injury required under the Robinson-Patman Act which is simply that the discrimination "may be to substantially lessen competition." The burden of proof would change from the existing reasonable possibility injury may occur to proof of actual injury.

B. Definitional Objections

In addition to the above conceptual problems, opponents of the reform proposals objected to a number of definitional difficulties which, it was felt, would require extensive litigation to clarify, and would abandon the definitional case law presently available under the Robinson-Patman Act.

As noted above, Commissioner Hanford felt that the definition of below cost pricing was too rigid and would restrict the FTC's ability to respond to new predatory strategies. Commissioner Nye, however, found that other terms were so vague as to require definition through litigation, with the result of burdening those seeking relief from formerly prohibited practices. 423/

> In the first place, I sense from the text of both drafts the desire to "clarify" the rules with

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422/ Testimony of Ernest G. Barnes, Subcommittee Hearings, pt. 2 at 173.

423/ Prepared statement of Stephen Nye, Subcommittee Hearings, pt. 3 at 101. (footnotes omitted).

respect to discriminatory pricing. While this desire is laudable, I fear the effort comes much too late. The courts, the Commission and other authorities have given substance to the language of the Robinson-Patman Act for almost forty years, and countless ambiguities have been resolved. Those which remain are far too few to justify throwing out the vast body of interpretive law which now provides a common understanding for most of the provisions of the Act. I do not claim that all the decided cases can be reconciled, nor do I mean to minimize the difficulty of predicting with certainty the outer limits of permissible conduct under the law. Once a business decision is made to attempt to depart from price equality, the particular marketing situation involved may well present the seller with a "maze of technical requirements." I am still not even certain, for example, whether a new entrant in a market can, for a while, price lower there than elsewhere. However, I must ask how many judicial decisions will be required to explain what it is to "overtly threaten" under Section 2 of the proposed Reform Act? Is it akin to conduct which "clearly threatens" under Section 5? Is a "section of the country" the same as a "geographical (but not product) market?"

Similarly, the attempt to treat disguised price cutting, such as brokerage and promotional allowances, as overt discounting was criticized as hopelessly complicating the formerly simple definition of "price". 424/

In enforcement in both kinds of cases, at the outset, it would appear to be an extremely dubious process to try to identify what in fact a seller's price is, under the so-called Reform Statute's definition of terms. By defining price as including allowances, services, facilities and the like, any attempt to identify a discriminatory price for enforcement purposes requires calculations--challengeable at every point--involving, first, a deduction of various promotional allowances from invoice price, then a coordination of allowances to customer services provided or performed--and this uncertain amount added back--together with a further deduction for whatever value might be deemed to apply to merchandising services or facilities granted by the seller.

Because a net price is virtually impossible to ascertain, when varied and complicated by these

424/ Testimony of Bartley T. Garvey, Subcommittee Hearings, pt. 2 at 165.

kinds of hidden discounts, the Robinson-Patman Act was, in large part, designed to deal separately with hidden discounts in the form of promotional and merchandising grants, and to force discriminations in price out in the open where they could be definitively addressed. That approach remains valid and necessary.

C. Favorable Responses

Many of those who were critical of the draft proposals nevertheless felt that the review of the Robinson-Patman Act prompted by the draft proposals was appropriate. Thus, Commissioner Nye felt that the present statutory scheme should not be "considered set in concrete. . . ." 425/ And Commissioner Hanford, while generally opposing the reform statutes, commented: 426/

> The legislative measures submitted to me by the Subcommittee concerning proposed repeal of the Robinson-Patman Act have, I think, stimulated a dialogue which will promote a meaningful interchange of ideas in the discrimination area. I am receptive to well-reasoned arguments for reform and, therefore, welcome this debate.

Favorable substantive comment came from F. M. Scherer, Director of the FTC's Bureau of Economics. While objecting to some of the above-noted definitional problems, Mr. Scherer approved the two proposals' attempt to reach only that conduct which presents a substantial risk of immediate, adverse impact on market structure, in contrast to the Robinson-Patman Act's approach of outlawing practices which have the remote potential of such impact: 427/

> The proposal does have some laudable features. The emphasis in Section 5(a) and (b) on discrimination

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425/ Prepared statement of Stephen Nye, Subcommittee Hearings, pt. 3 at 103.

426/ Prepared statement of M. Elizabeth Hanford, Subcommittee Hearings, pt. 3 at 78.

427/ Prepared statement of F. M. Scherer, Subcommittee Hearings pt. 2 at 148.

which is "significant in amount," "part of a pattern which systematically favors large recipients," and "clearly threatens to eliminate . . . competitors" would help discourage cases which have only a trivial adverse impact on competition.

Mr. Scherer also approved of the reform proposals' treatment of cost justification, as being more nearly consistent with economic theory than the present approach: 428/

> The cost justification provisions of Section 7 appear to be a major improvement, permitting the recognition of real efficiencies where they exist without imposing excessively costly accounting burdens upon potential respondents.

There were those who felt that, while the draft proposals accomplished some necessary reforms, even the limited regulation of the Department positions created a danger of discouraging vigorous price competition in the attempt to satisfy those who felt that some regulation of pricing was desirable. Thus Professor William F. Baxter of Stanford Law School was wary of any attempt to regulate pricing which is perceived as predatory: 429/

> I guess I have my own doubts whether the cost of even the more limited statute that the Justice Department has proposed on primary line may not in the end turn out to exceed any social benefits that it produces, but that at least is a close judgmental question.

The dangers of overreaching, even under the limited proposals, were again stressed by Professor Baxter: 430/

> Most certainly you could reach all [predatory pricing] you should reach under the proposed

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428/ Id.

429/ Testimony of William F. Baxter, DCRG Hearings Tr. 39.

430/ Id. at 58.

> statute that the Justice Department has drafted.
> I would say about 110 percent.

Objections to and support of the Department of Justice draft proposals, other than technical comments, traced the arguments for and against the Robinson-Patman Act. To the extent that the proposals would decrease the protection of the present statute, the Act's supporters saw the draft as repeal legislation and expressed the appropriate objections. The debate fostered by the reform proposals, therefore, provided a forum both for a refinement of the Robinson-Patman Act analysis and an example of the difficulties attendant upon revising a statute with such difficult goals.

Appendix E: LIST OF WITNESSES

Baker, Donald I.,
Assistant Attorney General, Antitrust Division, Department of Justice; formerly Professor of Law, Cornell Law School.

Baxter, William F., Professor of Law,
Stanford Law School; Brookings Institution; White House Task Force on Antitrust Policy (1969).

Bennett, Martin F.

Bison, Henry Jr., National Association of
Retail Grocers of the United States

Campbell, Christian L.,
Attorney, law firm of Sidley & Austin

Elzinga, Kenneth G., Professor of Economics, University
of Virginia

Fox, Louis, President, Associated
Wholesale Grocers, Inc.

Frederick, Donald A., National
Council of Farmer Cooperatives

Fricano, John C., member, law firm of Skazzen & Arps; formerly Chief of
Trial Section, Antitrust Division, Department of Justice

Friedlander, Philip P., National Tire
Dealers and Retreaders

Jones, William K., James Dohr Professor of Law, Columbia
University School of Law; New York Public Service Commission

Kauper, Thomas E., Professor of Law, University of Michigan Law School;
formerly Assistant Attorney General, Antitrust Division, Department of Justice

Kintner, Earl W., member, law firm of Arent, Fox, Kintner, Plotkin & Kahn;
formerly Chairman, Federal Trade Commission

La Rue, Paul H., member, law firm of Chadwell, Kayser, Ruggles, McGee
& Hastings; chairman Robinson-Patman Act Committee, Section of Antitrust law, American Bar Association

Lewis, John, National Small
Business Association

McKevitt, James D., National
Federation of Independent Business

Rogers, Watson, National Food
Brokers Association

Rothwell, Thomas A.,
Attorney, law firm of Pope, Ballard & Loos

Turner, Donald F., Professor of Law, Harvard Law School; formerly
Assistant Attorney General, Antitrust Division,
Department of Justice

Wiegand, Douglas, Menswear
Retailers of America

Woods, William E., National
Association of Retail Druggists

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