PRICE DISCRIMINATION LAW:

DEVELOPING A POLICY FOR NEW ZEALAND

A thesis
submitted in partial fulfilment
of the requirements for the Degree
of
Master of Commerce with Honours
in Accountancy
in the
University of Canterbury
by

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University of Canterbury
1985
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ABSTRACT

The purpose of this thesis is to develop a policy towards anti-competitive price discrimination in New Zealand. Price discrimination occurs where the ratio of price to cost in two sales differs.

Legislation against price discrimination may be enacted as part of our Competition Law, a set of laws designed to promote efficiency and competition in industry and commerce.

The first section of this thesis examines the economics of price discrimination and its effects on efficiency, income distribution and competition. We conclude that the effects are ambiguous and depend upon the circumstances in which the discrimination is practiced. However we conclude that systematic price discrimination can be harmful to competition, whilst unsystematic price discrimination can promote competition and that there are a priori grounds for anti-price discrimination legislation.

The second section examines specific approaches taken to price discrimination legislation. Particular emphasis is placed on the U.S. Robinson-Patman Act which is one of the most extensively litigated price discrimination laws in the world. A review of the implementation of this Act shows that it has failed to promote competition or increase efficiency. In fact, it has done more to inhibit these goals than promote them. We conclude that there are conceptual problems with anti-price discrimination legislation and this conclusion is reinforced by a study of the Australian price discrimination law. We therefore examine the conceptual framework in which price discrimination is controlled in other developed countries such as the United Kingdom, Canada, Eire, France, West Germany and the EEC. We conclude generally that price discrimination is a problem of monopoly and should be treated as such.
The final part of this thesis reviews price discrimination law in New Zealand and suggests a policy that would align the Commerce Act with our conclusion that legislation against price discrimination is undesirable.
CHAPTER I

PRICE DISCRIMINATION LAW: AN INTRODUCTION

1.1 COMPETITION LAW AND THE NEW ZEALAND ECONOMY

Central to the aims of the New Zealand economy is the maintenance of the well-being of New Zealand citizens. As in many other capitalist countries, this goal is achieved through a mix of competition and government intervention.

Competition is the underlying principle of our economy. A necessary part of competition is the freedom of individuals to trade. The individual is given the freedom to attain his personal goals and, in doing this, becomes part of the invisible hand which guides the allocation of resources in our economy. Through this process of free bargaining the welfare of the individual, given his limited resources, is maximised. Also through this process, scarce resources are allocated in the most efficient and effective way and this maximises the welfare of the nation as a whole.

However freedom does not necessarily lead to competition. This is recognised by all 'free' countries who have enacted antitrust laws. With complete freedom, market participants may contract to limit competition and market mechanisms may not be sufficiently sensitive to correct any defect in the competitive process. Thus laissez faire and competition are not synonymous. The result is the breakdown of the competitive process and the efficient allocation of resources.

One part of the solution to this problem is to legislate against monopolies and against contracts between industry participants designed to monopolise industry wherever these forms of monopoly threaten the well-being of the nation. This is the basis of our Competition Law or
Antitrust Law, (literally anti trust as these laws were enacted to curb the growth of powerful trusts in the United States around the turn of the century).

Competition is not always seen as a desirable goal in the short-term. For many years the New Zealand economy has been protected from foreign competition so that it may grow to a point where it can compete effectively with those foreign firms. Internal competition has also been stifled so that firms may, for a short period, devote resources to the development of their industry enabling them, in the future, to compete more effectively.

Nor is competition seen as the only goal. New Zealand has a history of egalitarian philosophy. Underlying many of our laws is a desire to protect the weak and the defenceless. There is a desire to protect the small firm and its employees from the insecurities of ruthless competition and to protect the consumer from the exploitation by powerful monopolies. Although these are secondary to the goal of competition and are often achieved concomitant with that goal, they do hold a special importance in our political and economic regulation.

All of these concerns are reflected in our Competition Law contained in the Commerce Act 1975. These multiple aims can be seen in the Long Title of the Act, the General Objectives of the Act contained in Section 2A, and the definitions of Public Interest contained in Section 21 and Section 80 of the Act. The Objects of the Act in 2A are reflective:

2A General objects—(1) ...the Commission, Examiner, and the Secretary shall be guided by the following objects:
(a) The promotion of the interests of consumers;
(b) The promotion of the effective and efficient development of industry and commerce;
(c) The need to secure effective competition in industry and commerce in New Zealand;
(d) The need to encourage improvements in productivity and efficiency in industry and commerce in New Zealand;
(e) The economic policies of the Government as transmitted from time to time to the Commission by the
Minister [of Trade and Industry] and as published by him in the Gazette.

The objectives are varied and often contradictory. They indicate that the protection of consumers and employees, and the development of industry and commerce are not to be gained solely by the promotion of competition, as is the prevalent theory in the United States. However, the Act is chiefly concerned with the promotion of competition and, with rare exceptions, the Commerce Commission has placed competition at the forefront of its objectives. To achieve these objectives, the Commerce Act proscribes certain monopolies, mergers and takeovers, and agreements to restrict trade, whenever they are contrary to the public interest.

1.2 WHAT IS PRICE DISCRIMINATION?

Price discrimination occurs where the ratio of price to marginal cost is not equal for all sales.

\[
\frac{\text{Price (1)}}{\text{Marginal Cost (1)}} \neq \frac{\text{Price (2)}}{\text{Marginal Cost (2)}}
\]

Price discrimination may occur over time, spatially, between goods, or between buyers. Price discrimination over time is generally hard to identify because of the interaction of many other factors affecting price and marginal cost, while to prevent price discrimination between different goods would require setting a constant profit ratio on all goods produced. The anti-price discrimination legislation is therefore predominantly concerned with price discrimination occurring spatially and between buyers.

'Price discrimination' conjures up a situation where one buyer is granted a discount which another, otherwise identical, buyer is not given. This is one obvious form of price discrimination. However the practice masquerades under a variety of other names and is more prevalent than might at first appear. Price discrimination may occur
where functional discounts are granted to buyers who are higher in the
distribution chain, (eg. a tradesman may receive a discount which is
unavailable to the ordinary consumer); where the same goods are sold
under a trade brand and under a private brand and the price differential
between the two products is unrelated to the cost differences in
advertising the brand; where all buyers are charged the same price for a
product regardless of whether a buyer requests delivery and another does
not; where products sold as a group or set are cheaper than the same
products sold individually; where theatre tickets are sold at a lower
price to some buyers than to others, etc. In fact, when one does
consider the number of instances where one buyer can purchase goods at a
lower price than another and that price difference is unrelated to the
difference in cost of providing the goods to the buyers, then one
realises that price discrimination is not rare at all, but rather found
in almost every part of our economy.

An initial reaction to price discrimination may be to claim that
certain people or groups are being treated "unfairly" and are
discriminated against. Perhaps this is true. Perhaps a pensioner should
be charged the same price as any other theatre-goer. However, it is not
the purpose of this thesis to evaluate price discrimination in terms of
political or social impact, but rather to consider the appropriateness
of price discrimination legislation as part of our policy to protect the
interests of consumers, employees, and to promote industry and commerce
through the promotion of effective competition. Hence analysis is
confined to the economic rather than the social aspects of price
discrimination.

1.3 PRICE DISCRIMINATION AND COMPETITION

The relationship between price discrimination and competition
is both interesting and complicated. An exploration of this relationship reveals why a proscription against price discrimination might rationally be found in competition laws.

Price discrimination is indicative of monopoly. Before a seller can discriminate between two buyers he must have sufficient monopoly power to influence prices in a market. If a competitive situation prevails in the market the seller can sell as much as he desires without dropping his price to some buyers. Nor may he raise his prices to other buyers without losing his sales. A parallel argument applies to the buyer with monopsonic power.

Even though price discrimination is indicative of a monopoly position, this does not mean that it should necessarily be proscribed. It is essential to remember that price discrimination is the symptom of the disease and not the disease itself. An evaluation of price discrimination according to the economist's criteria gives equivocal results. It has ambiguous effects on income distribution and efficiency. Price discrimination may affect competition but even here, the effect may be pro- or anti-competitive depending on the surrounding circumstances.

Price discrimination may be anti-competitive either because -

(i) it allows a seller to engage in predatory activities to destroy his rivals;

(ii) it is granted to some buyers and not to others which gives some buyers a competitive advantage and distorts competition at the buyer's level;

(iii) it is used to enforce another trade practice such as resale price maintenance;

(iv) a discriminatory pricing system facilitates tacit collusion between competitors.
(1) Price Discrimination and Predatory Pricing

The earliest concern with price discrimination was where it is used to fund a predatory activity. The argument runs that a seller uses higher prices in one market where he holds a monopoly to subsidize lower predatory prices in another market where he faces competition. By funding his predatory activities with monopoly profits he may destroy his competitors and extend his monopoly position. The injury is at the primary line, i.e. the competitors of the seller. This form of price discrimination was said to be the method by which Rockefeller extended the monopoly position of Standard Oil Co. (N.J.) Ltd.

Where price discrimination is linked with predation, the practice may be divided into three principal evils. The predatory low price which destroys competition and allows the monopolist to extend his market power, the monopolistic high price indicating that the monopolist is exploiting a second group of customers, and the subsidization of the low price by the high price, indicating that one group of buyers is subsidizing the purchases of another group.

(2) The Distortion of Competition at the Buyer's Level

Price discrimination may distort competition at the buyer's level, termed the secondary level. Where two otherwise identical buyers are in competition and one is able to buy goods at a lower price than the other, the disfavoured buyer is immediately placed at a competitive disadvantage vis-a-vis the other buyer. The favoured buyer may then grow (possibly into a monopoly position) for reasons unrelated to efficiency. In this way, secondary level competition is distorted.

The effect of a price discrimination may be felt at levels further down the distribution chain. The favoured buyer may pass on some or all of the discount to his customers and this may distort competition...
at the tertiary level or even beyond. Even where the discount is not
passed on to customers of the buyer, the economic dislocation at the
secondary level will have a flow-on effect causing further dislocation
at lower levels of distribution.

The buyer able to induce such discounts is generally the large
buyer, the monopsonist. Often the monopsonist is a chain store or mail
order firm. These types of firms attribute their advantages to the
economies of high volume low profit merchandising, the elimination of
the middleman, and discounts gained through greater buying power. These
advantages allow lower retail prices. It is not surprising therefore that
most support for anti-price discrimination legislation comes from the
small retailers and redundant middlemen. These sector groups have
concentrated their attacks on those discounts gained not because of the
efficiency of the large buyer but because of the abuse of buying power.
For this reason, anti-price discrimination legislation is often as much
protectionist legislation as it is competition law.

(3) **Price Discrimination Employed to Support Another Trade Practice**

Price discrimination may affect competition where it is used to
support an anti-competitive agreement. Discounts may be granted to a
buyer who conforms with the policies of the seller. In these cases, the
discrimination is only ancillary to another trade practice. The
evaluation of competitive effect centres on the main practice rather
than the discrimination, which is important only in as much as it
represents the means of sustaining the main offence.

(4) **Price Discrimination to Support Horizontal Collusion**

Price discrimination may also occur in the form of a pricing
system, usually a delivered pricing system. These systems ease the
problems of collusion and facilitate horizontal price agreements within
an industry. Breaking up the pricing system is the first step towards destroying the price fixing. In these cases analysis centres on whether the discriminatory pricing facilitates agreement between industry participants. The trade practice is horizontal in nature, although it is often not reached under the conspiracy laws because the collusion is tacit and not express.

1.4 PRICE DISCRIMINATION LEGISLATION IN NEW ZEALAND

In an attempt to limit primary and secondary line injury resulting from price discrimination many countries, including the United States, Australia, Canada and the EEC, have enacted anti-price discrimination legislation. However, there is no equivalent law in New Zealand. Why is this when there has been legislation in the United States since 1914?

One of the main reasons is that supporters of price discrimination law has been motivated by its protectionist appeal rather than its pro-competitive effects. Small retailers and wholesalers have remained strong in New Zealand and have not needed to react so vigorously against the chain-stores. We might expect that in the future increased concentration and more vigorous competition will lead to demands for price discrimination legislation.

1.5 THE OBJECTIVE OF THIS THESIS

This thesis preempts such demands and answers whether price discrimination should be legislated against, and, if so, whether it is possible to legislate against undesirable price discrimination without such legislation itself causing deleterious effects. These two questions are inter-related and, as shall be seen, the second question answers the
1.6 THE STRUCTURE OF THIS THESIS

The thesis is structured to answer these questions. The first part examines price discrimination in economics, giving a detailed analysis of price discrimination and its effects. The purpose is to determine whether, in theory, it is desirable to legislate against price discrimination.

The second part examines the history, implementation and impact of the U.S. Robinson-Patman Act which is, without doubt, the most extensively litigated, analysed and criticized price discrimination law enacted today. The purpose of this part is to reveal the immense difficulties associated with price discrimination law and to determine whether price discrimination law contributes to a more efficient and competitive economy. The conclusion is that the Robinson-Patman Act has had undesirable effects on competition and efficiency and contains formidable, indeed, insurmountable problems of implementation.

The next part considers comparative approaches to price discrimination. Particular attention is given to the Australian approach because this represents an attempt to improve on the direct approach of the Robinson-Patman Act, and also because legislative changes to New Zealand antitrust laws may well be based on the Australian approach.

The final part outlines the current legislation pertaining to price discrimination in New Zealand, as well as the proposed legislative amendments. It concludes with suggestions as to the appropriateness of price discrimination law and recommendations for future New Zealand legislation.
1.7 PRICE DISCRIMINATION AND THE PROTECTION OF SMALL BUSINESS

Price discrimination law is considered in light of the objective of maximising efficiency and competition in an economy. Yet price discrimination is often seen as legislation to protect small business.

The protection of small business is outside the scope of this thesis. Nevertheless it is possible to draw some poignant conclusions about the effect of price discrimination legislation on small business. Price discrimination law gives minimal, if any, benefit to small business, and in many instances may actually cause harm. Nor can a law against price discrimination appreciably halt any trend towards increased concentration or affect the competitiveness of small business. If protection of small business is seen as the goal, then some other means of achieving this goal should be found.

Nevertheless, it shall be seen that many countries have enacted price discrimination legislation in response to the political pressure of small business groups. Pressure may also come from such groups in New Zealand. It must be remembered that the decision to enact price discrimination legislation may be influenced more by political lobbying than by rational thought.
CHAPTER II

THE ECONOMICS OF PRICE DISCRIMINATION

Competition law is derived from economic theory and it is this theory that should govern our approach to price discrimination. The purpose of this chapter is to provide a theoretical model of price discrimination enabling us to study its effects on income distribution, efficiency and competition, to identify forms of price discrimination practiced in our society and to establish whether these forms ought to be subject to judicial review. The practical problem of implementing anti-price discrimination law is delayed until Chapter 3, while Chapter 4 examines the extent that a law can succeed in delineating and preventing undesirable price discrimination. Over the next chapters, the reader should bear in mind the extent that the economic and legal definitions of undesirable price discrimination over-lap as in the final analysis the law against price discrimination is based on economic theory.

This chapter is divided into three sections. The first outlines the theory of price discrimination. The second provides categories of price discrimination. Particular attention is paid to those forms commonly found in industry and commerce which have an impact on competition. The third section provides the economic rationale for preventing systematic (but not sporadic) price discrimination.

2.1 DEFINING PRICE DISCRIMINATION

(1) Definition and Conditions for Price Discrimination

No simple definition of price discrimination is available. However, it is satisfactory to say that price discrimination is the sale
of different units of a good or service by a single seller at price differentials not directly corresponding to differences in supply cost. This definition includes the sale of identical product units to different customers at different prices, the sale of identical units to the same customer at different prices, and the sale of units at different prices, where the difference in the cost of supplying these units does not correspond to the price differential.

Three conditions must exist before a seller can engage in price discrimination. A seller must have a degree of market power. If a seller operates in a market where there is perfect competition then, ipso facto, he can sell as much as he wishes at the competitive price, he can sell nothing at any higher price, and he has no reason to sell at some lower price (except perhaps for altruistic reasons). If he sold at a price below competitive price he would no longer be earning a normal rate of return. Second, the would-be discriminator must be able to segregate his customers into groups with different price elasticities of demand, or into discrete classes with varying reservation prices. Third, opportunities for arbitrage, resale by low-price customers to

---


2 'Cost' refers to the economic and not the accounting concept of cost.

3 See Scherer, op. cit., p. 253; Phlips, op. cit., p. 14-16. Phlips identifies four conditions. The second and third conditions are combined in Scherer's second requirement.

4 The reservation price is the price which a buyer is prepared to pay for one additional unit of a good or service.
high-price customers, must be constrained.

(2) Theoretical Forms of Price Discrimination

Three main price discrimination classes can be distinguished, first degree (perfect), second degree, and third degree (block pricing).

(a) First Degree. With first degree price discrimination, each unit is sold at its reservation price. In this way, each customer is charged the maximum price that he is prepared to pay for each additional unit. The seller produces at the level that would prevail under perfect competition (\(X_C\) in Fig. 2.1) and thus the output is greater than under monopolistic one-price conditions where the output is \(X_m\). All consumer surplus (represented by triangle \(ABP_C\)) that would have gone to consumers under conditions of perfect competition goes to the seller.

![Output Under Conditions of Perfect Price Discrimination](image)

(b) Second Degree. First degree price discrimination is an

5 prohibitive transport costs and other costs of resale, the non-transferable nature of some personal services such as medical care, or direct supervision by the seller such as identity cards, are all factors preventing arbitrage.
abstraction that is rarely found in practice. Second degree price discrimination is similar except that the seller sets n different prices such that all units with a reservation price higher than the highest price set by the seller \( (P_1) \) are sold at that price, (in Fig. 2.2, \( 0 - X_1 \) units are sold at price \( P_1 \)). All remaining units with a reservation price higher than the second highest price set by the seller \( (P_2) \) are sold at that price, etc. This is shown in Fig. 2.2.

**Fig. 2.2 Second Degree Price Discrimination**

![Diagram of Second Degree Price Discrimination](image)

Again, the output exceeds that which would have resulted under monopolistic conditions but most of the consumer surplus that would have resulted had \( X_8 \) units been sold at a competitive price is transferred to the seller.

*(c) Third Degree.* Third degree price discrimination differs fundamentally from the previous two types discussed. A monopolist who must charge a uniform price to a single group of buyers will maximise his profits by setting price \( P \) according to the intensity of demand of that group:

\[
MR = P - \frac{P}{e}
\]

where \( P \) = Price
MR = Marginal Revenue
\( e \) = Price elasticity of demand.

Where the monopolist supplies two groups, each with a different
elasticity of demand, then the monopolist maximises profits by equating the marginal revenue gained from each market and hence charges different prices to each group. This is shown in Fig. 2.36.

Fig. 2.3  Block Pricing

2.2 CATAGORIZING PRICE DISCRIMINATION

The theoretical models of price discrimination do little justice to the varieties and complexities of price discrimination practiced in our society. Scherer usefully provides a catalogue of the many forms of price discrimination, divided according to whether the discrimination is based on personal characteristics of the buyer, characteristics of the group or class of buyers, or characteristics of the product itself\(^7\).

(1) Personal Discrimination

(a) Haggle-every-time. Each transaction is a separately

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\(^6\) Taken from Scherer, *op. cit.*, p. 255, Fig. 10.2.

negotiated bargain. Examples include the typical Middle-Eastern bazaar.

(b) *Give-in-if-you-must.* Secret departures are made from price lists when buyers play one seller off against the others. An example of this is the U.S. gypsum board industry, recently the subject of antitrust litigation. The sellers' industry was oligopolistic and the sellers produced a homogeneous product. Hence sales were very sensitive to price variations. Buyers would attempt to gain price concessions from one seller by claiming that they had received concessions from other sellers. The antitrust litigation arose out of the sellers' attempt to maintain high price levels by verifying amongst themselves whether secret concessions were, in fact, offered.

(c) *Size-up-his-income.* Wealthier customers with inelastic demand are charged more than the less affluent, who, at high prices, would restrict consumption disproportionately. An example is the stand-by concessions which were once offered to students by Air New Zealand, but were denied to the normal traveller, (eg. the business person), with an inelastic demand.

(d) *Measure-the-use.* Customers who use a good or service more intensely are charged more, even though differences in costs may be negligible. Telser argues that IBM's attempt to extend its monopoly position from tabulating equipment to punch cards using a tying agreement represents this form of price discrimination. By receiving its monopoly revenues from the cards rather than from the machines, IBM was able to gauge which customers used the machines more intensely and charge them a higher price than others with lower demand.\(^8\)

(2) **Group Discrimination**

(a) *Absorb-the-freight.* There are several types of price

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discrimination involving the absorption or over-charging of freight to customers located at varying distances from one's production site. These examples of delivered pricing systems will be discussed in more detail later.\(^9\)

(b) Kill-the-rival. Prices are systematically reduced, perhaps below cost, only in a market served by a rival the discriminator is trying to drive out of business. This form will be discussed in more detail later.\(^10\)

(c) Dump-the-surplus. Goods temporarily in excess supply are offered at reduced prices overseas so as not to depress the domestic market. Scherer cites the U. S. Food for Peace program during the early 1960's as partly motivated by this reason.

(d) Get-the-most-from-each-region. Prices are persistently held higher in regions where competition is weak than where it is strong.

(e) Promote-new-customers. New customers are offered lower prices than those paid by established customers in the hope of developing brand loyalty. Magazines are avid practitioners of this art, offering new subscriptions at prices a fraction of what old subscribers pay.

(f) Favour-the-big-ones. Large buyers are granted systematic price concessions exceeding the cost-savings associated with volume transactions.

(g) Protect-the-middleman. Large retailers who incur the cost of performing their own warehousing and distribution functions are charged the same prices as retailers who buy from wholesalers in an attempt to protect the middleman from competition through vertical integration.\(^11\). The Robinson-Patman Act was motivated by this reason.

\(^9\) infra, p. 29.

\(^10\) infra, p. 25.

\(^11\) See the discussion on functional discounts, infra, p. 22.
(h) **Hold-them-in-line.** Retailers who fail to comply with a manufacturer's list price suggestions are denied special discounts granted to those who conform.

(i) **Divide-them-by-elasticity.** Group discrimination may also be practiced whenever groups readily classifiable by age, sex, occupation, etc. have different reservation prices or demand elasticities. For example, lower prices are charged for children's haircuts (despite the higher labour input in shearing a wiggling object) because of the stronger 'do it yourself' competition.

(3) **Product Discrimination**

(a) **Appeal-to-the-classes.** Differences in price more than proportional to differences in cost are associated with premium quality. For example, much higher margins between price and incremental production cost are realized on clothbound as opposed to paperbound books.

(b) **Make-them-pay-for-the-label.** Manufacturers distribute a physically homogeneous product under various brands, charging more for better-known labels. The shelves of chain-stores contain many examples of private-label goods sold cheaper than the same goods carrying a brand-label.

(c) **Clear-the-stock.** Price concessions are granted at special times of the year, or continuously in special sections of a retail store, in order to reduce inventories or increase sales to customers with weak budgets and strong elbows.

(d) **Switch-them-to-off-peak-times.** Lower prices are charged for services identical except with respect to time of consumption in order to encourage fuller and more balanced utilization of capacity. Toll-call charges are an example of this form of discrimination.

(e) **Get-the-most-from-each-group.** In this final catch-all
category we include such practices as charging higher railroad freight rates on commodities valuable relative to their weight; offering additional blocks of electricity at lower rates to encourage homeowners to install electric heaters and heating systems; and the realization by multi-product firms of higher price-cost margins on items for which demand is relatively inelastic than on those with highly elastic demand. In this category we might also include skimming - introducing a new and superior product at a high price designed to extract the highest possible revenue from persons with high reservation prices, and then gradually reducing the price to penetrate a broader market.

2.3 PRICE DISCRIMINATION IN INDUSTRY AND COMMERCE

The reader will no doubt have recognised many of the forms of price discrimination listed. Some of these forms, (and some cases where price differentials are granted yet there is no economic discrimination), found in commerce and industry have received special attention in antitrust litigation. It is useful to identify these pricing systems and discuss their economic significance.

(1) **Quantity and Volume Discounts**

A quantity discount can be defined as a discount given due to the quantity purchased at any one time by a buyer or group of buyers. A volume discount is based on aggregate sales by a buyer or group of buyers over a period of time, (usually a year). A 'retroactive' discount schedule allows the highest discount rate to be applied to all sales in a period while a 'non-retroactive' schedule bases discounts on

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13 *ibid*, p. 932-933.
volume purchased up to that point in time in the period. Generally discounts are available to buyers who pool their purchases, and no distinctions are made between buyers who operate at different functional levels of distribution.

Quantity discounts theoretically reflect the cost-savings that accrue to the seller from the large order sizes made by the buyer. Examples of cost savings might be lower packing and delivery costs, or lower processing and collection costs. Volume discounts may also be justified by cost-savings that accrue to the seller, although the source of these cost-savings is less obvious. Examples might be cost savings achieved through better production planning, steadier production levels, and assured sales.

In as much as quantity and volume discounts are cost-justified, they are not forms of economic price discrimination. However, because it is generally the large buyer that receives these discounts, they may in fact be special discounts to large buyers and may not be cost-justified at all. Thus they are simply 'favour-the-big-ones' forms of discrimination and may have an exclusionary effect at the primary level and distort competition at lower levels.

(2) Functional Discounts

Rowe defines a trade or functional discount:

The seller's schedule fixes discounts from quoted price to buyers classified according to rank on the distribution ladder. Typical systems allow reductions to wholesalers, jobbers, and retailers in decreasing amounts, regardless of the size of individual transactions or aggregate sales volume. A wholesaler may buy ten units during one year. But a retailer who buys 100 units each month must pay a higher price.


A seller may grant a functional discount for several reasons. One is that a buyer may relieve the seller of several functions which the seller would otherwise have had to perform. The functional discount recognises the value of these services. It is therefore a type of cost-justified discount passed to the buyer.\(^{16}\)

Conceptually the functional discount or trade discount represents economic recognition by the manufacturer of the value of distributive services performed by types of marketing intermediaries. These services include warehousing, delivery, the cost and risk of servicing small, scattered accounts and other such functions.

The functional discount system prevents price competition at the lower levels of distribution that is unfair due to disproportionate pricing by the manufacturer. In this way, the retailer buys at the same price no matter who performs the wholesale functions. To illustrate, suppose the manufacturer gives a $2.00 functional discount if the buyer performs the delivery function. Suppose also the cost (economic cost) of performing this function is $2.00. Then no matter if the manufacturer performs the function for the direct-buying retailer, the wholesaler performs the function for the indirect-buying retailer, or the direct-buying retailer performs the function himself, all retailers will purchase the product for the same price.

This raises two questions. Should the functional discount be related to the cost savings of the manufacturer or the costs incurred by the person who performs the function? If the buyer (whether the direct-buying retailer or the wholesaler) can perform the function for less than the functional discount, and the discount is related to the cost savings of the manufacturer, than some retailers may purchase the goods at a lower price. Although according discounts in this manner leads to greater efficiency, it destroys the equal footing that existed between

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retailers. If the discount is related to the costs of the buyer, than all buyers purchase the goods at the same price, however, inefficient distributors are shielded from competitive pressures through the subsidization by the manufacturer and this creates inefficiency.

The second question is how to identify the functional level of the buyer. Usually this is done simply by looking at the primary functions of the buyer. Thus a direct-buying retailer may still be classed as a retailer even though he buys from the manufacturer and performs the wholesale function himself. Alternatively, the buyer may be classified according to the level at which he buys the goods, the level at which he resells the goods, or the functions he performs. Although this last classification method is consistent with the concept of the functional discount, it is the one which is least used.

This suggests that there may be other reasons for the functional discount. One such reason is to protect the manufacturer-wholesaler-retailer distribution channels from competition from the more modern vertically-integrated firms, typically the direct-buying retailers, (although the direct-buying consumer is an even more pronounced example). This is a form of 'protect-the-middleman' price discrimination and has the added effect of protecting the small retailers who buy from the middleman.

A third explanation links functional discounts with volume discounts. The manufacturer grants a functional discount to a class of buyers because it is desirable to sell to these high quantity purchasers. Although in the short-run their purchases may be small, in the long run the patronage of this class may allow the manufacturer to utilize his productive resources to a greater extent.

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(3) Promotional Discounts

The promotional discount can be seen as a short-term discount given to a class of buyers in order to induce them to purchase a product with the hope that an introduction to the product will create brand-loyalty and generate future revenues. Promotional pricing requires a degree of brand or product differentiation. Price discrimination usually occurs in conjunction with promotional pricing as the seller is usually an established seller who confines his discount to selected new markets.

Promotional pricing is one of the most effective techniques available to the new entrant to tempt buyers away from their present brand allegiances. Promotional pricing is seen as desirable where it increases the number of sellers and the variety of goods available in a market, and where it occurs in a tightly oligopolistic industry where any price competition is seen as desirable.

It may be anti-competitive where it injures other sellers. This may occur where the promotional price is excessively low or continues for a long period of time. (A promotional price may, in fact, be intended as a predatory price). It may also distort secondary line competition, especially where it simply re-allocates market shares between sellers (and hence between intermediaries) and does not increase overall sales. Because of its potentially harmful nature, promotional pricing has often been attacked under price discrimination legislation as a form of predatory pricing.

(4) Predatory Pricing

A seller seeks to drive his competitors from the market by engaging in, or threatening to engage in predatory activity. After lowering his price to a predatory level and destroying his opponents, he raises his price to a monopolistic level and recoups his losses. However,
the classical image of the large predator destroying his weaker rivals has been questioned, with the implication that there is no need for any law covering predatory activity. McGee originated this claim in his empirical study of *Standard Oil Co. of N.J. v. United States*\(^{18}\).

Examining the trial records, he concludes that, contrary to popular belief, there was little direct evidence of predatory action, the prosecutions case being based more on subjective interpretation than objective analysis.

McGee strengthens his claim with a theoretical model which illustrates that while predation is possible, it is a costly and irrational method of monopolising the market. He shows that, for a predatory activity to be successful, the seller must drastically reduce his price to compel a rival to exit the market. As the rival's market share declines, the predator's share increases and this increase in sales serves to magnify any loss that results from his price reduction. Even if the seller in the short term successfully compels his rival to cease sales, the rival's assets remain intact and the rival can continue operations after the predator raises his price to recoup lost profits. It is also unlikely that there would be barriers to entry adequate to prevent the entry into the market of new competitors.

Instead of predation, the seller has other more attractive alternatives such as direct collusion or takeover of rivals. Merger is a cheaper, quicker, and more permanent method of securing a monopoly position\(^{19}\).


\(^{19}\) McGee does not consider any restriction that merger laws may have on the policy of the predator.
McGee's paper was quickly followed by others of the same vein. However, Yamey provides alternative considerations which may suggest why a seller may prefer predation to merger. A direct merger may not always be advantageous because the rival may recognize the value in the form of monopoly profits of the merger to the large competitor. Predation, or the threat of predation, may cause a rival to accept a lower merger price. A merger policy may also encourage new entrants to enter the market in order to be 'brought up' by the monopolist and in this way obtain some of the seller's monopoly revenues. A brief period of predatory prices may serve to discourage these new entrants. Yamey's major contention, however, is that the price cut need not be 'below cost' in order to convey the message to the rival. Thus, while predation may involve opportunity losses, it need not involve actual losses. For this reason, the predator may be able to sustain the low price for a longer period and at lower cost than if he embarked on a course of drastic price-cutting.

Other reasons have been offered to explain why predatory behaviour may be a rational policy. Predation may destroy a less efficient firm. Here again the monopolist's price need not be below his costs in order to drive his competitor from the market. Another argument has been developed in the scenario of an industry characterized by economies of scale. A seller may produce at a level such that his output, along with the output of a new entrant (at the new entrant's


minimum level of efficiency), exceeds the demand for the product. The potential new entrant, seeing that he will not be able to produce at efficient levels, is discouraged from entering the market. Again the seller need not incur a loss in order to maintain his monopoly position.

However, there has been a resurgence of the view that it is not necessary to legislate against predatory pricing, even though such pricing may be rational from the view of the monopolist and undesirable from the view of the public. The reasons for this view are summarized:

(i) Withstanding predation may be profitable for the victim when there are monopoly profits to be made in the market, and the victim therefore has a strong incentive to stay.

(ii) Capital markets are sufficiently perfect to sustain a victim (or his assets) during profitable resistance.

(iii) Losses during a price war will be proportionally higher for the predator than the victim. The predator must expand output at ever-increasing costs to hold down the market price, while the victim may reduce output or even shutdown altogether for a period and thereby reduce costs.

(iv) The illegality of mergers to effect monopoly will block purchase of the victim by the predator, so the price war will have to last the useful life of the victim’s assets to drive them from the industry, becoming all the more costly.

(v) If the victim is driven from the market, investors will purchase the victim’s assets at depressed prices caused by the price war, keeping them available for continued production.

(vi) Entry and exit barriers will be symmetrical. Thus, the predator will find it difficult to drive out a highly capitalized firm.

while quick exit of firms with proportionally high variable costs will bring quick re-entry (or new entry) when the prices are once again raised to monopoly levels.

(vii) The anticipated monopoly returns are pushed into the future, the less will be their present value, and the less likely will predation be found profitable in light of short-run losses and sacrificed profits. Moreover, the risk associated with uncertainty about other future economic conditions will reduce the present value of future monopoly returns.

(viii) The victim can enter into long term contracts with customers at some price that is more attractive than the monopolist's offer of temporary low prices to be followed by monopoly prices.

(5) **Delivered Pricing**

The seller may quote prices at the point of origin, termed the free-on-board price (f.o.b.) or net-mill price, or he may quote prices inclusive of transport costs, this price termed the delivered price. Whichever pricing system is adopted, if the price reflects both the transport costs (if paid by the seller) and the cost of the goods, then there is no economic discrimination. But where this is so, the seller has a competitive advantage with buyers situated near him and a competitive disadvantage with those buyers situated closer to a rival seller. This is shown in Fig. 2.424. Line A represents the cost of goods and transport of a seller situated in Auckland and line W represents those costs for a seller in Wellington. \( P_a \) and \( P_w \) represent the normal sale price of the good for a buyer located in Auckland and Wellington respectively. Costs and prices are presumed to be the same for both sellers.

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24 Fig. 2.4 is adapted from Scherer, *op. cit.*, p. 264.
(a) **Uniform Delivered Pricing.** Clearly a seller in Wellington can offer better prices to any buyer situated south of Taupo, and an Auckland seller can offer better prices to those buyers north of Taupo. Thus only in Taupo will the two sellers compete. If the Wellington seller lowers his price for the goods to \( P_w' \) in order to entice a buyer in Hamilton, this price cut will be quickly met by the Auckland seller\(^{25}\). Neither seller would benefit from such a price cut as the long-run as total prices fall to \( A' \) and \( W' \) and only the buyers benefit.

The two sellers would be better off recognising their interdependence and offering a uniform price (\( P \)) to all buyers. For buyers who purchase from the Wellington seller, those located in Wellington must pay a higher price for the goods (ie. they are charged 'phantom freight'), while those closer to Auckland would pay a lower price (ie. 'freight absorption' occurs).

(b) **Basing-point Pricing and Multi-basing-point Pricing.** Alternatively the Wellington seller could adopt Auckland as a basing-point and calculate all prices as though the goods were delivered from Auckland. Thus he effectively adopts the price schedule of the Auckland

\(^{25}\) Also the Wellington seller may be prevented from lowering his price only in a small geographic area if the business in that area is low compared to the business in other areas and buyers in those other areas pressure for uniform price reductions.
seller. Again, buyers nearer to Wellington are charged phantom freight and there is freight absorption when the buyer is situated closer to Auckland.

A variation of the basing-point system is the multi-basing point system, where two or more basing-points are established (say, in Auckland and Christchurch) and the seller calculates prices as though the goods were shipped from the basing-point closest to the buyer. (Thus a Timaru buyer would be charged for goods plus transportation costs from Christchurch, even though the goods may have been shipped from Auckland or Wellington). Generally the plant-sites of major competitors are used as basing-points as this allows all sellers to quote the same prices as those competitors.

(c) **Freight Equalization.** Freight equalization is similar to the basing-point system except the basing-point is not fixed. Instead freight is determined as the cost of transporting the goods to the buyer from the location of the seller which is nearest the buyer.

(d) **Zone Delivered Pricing.** Zone delivered pricing is a variant of uniform delivered pricing. The country is divided into zones and a uniform price is charged to all buyers within a zone. This price is generally the price of the good plus the average cost of transporting goods to buyers in the zone.

Under each of these systems, the price charged to the buyer does not reflect the price of the good and the true cost of transport. Therefore each is a form of price discrimination. These systems are usually employed where the product is homogeneous (thus the buyer may switch sellers without incurring any cost), and the freight charges are a significant cost of the good, (thus the buyer is sensitive to the amount of freight he pays). The steel industries in Europe and the United States have commonly used basing-point delivered pricing.

(e) **Effects on Competition.** Each system may have pro- and anti-
competitive effects depending on the circumstances in which it is employed. At the seller's level, these systems allow sellers to compete in distant areas despite the inhibiting factor of high transport costs and this has a pro-competitive effect. A delivered pricing system may be pro-competitive where there is a horizontal price-fixing agreement between sellers. Under an f.o.b. system if a buyer switches suppliers, it is immediately apparent that the seller must have offered some price inducement. But under a delivered pricing system, a buyer receives the same price quotations from every seller and it is harder to infer why a buyer might switch suppliers. Thus a delivered pricing system may allow sellers to shade cartel prices yet remain undetected.

On the anti-competitive side, delivered pricing systems are susceptible to abuse as means of supporting collusive action aimed at price stabilization. A uniformly maintained industry-wide pricing system simplifies each seller's pricing structure and eases the task of policing and supervising a price fixing agreement. Even in the absence of direct collusion, a delivered pricing system may encourage parallel behaviour with each seller safe in his knowledge that other sellers are pricing at the same level as him. Zone delivered pricing may be used to limit entry to a market of a prospective seller by identifying his customers and offering a low price confined to their zone.

At the secondary level, uniform delivered pricing destroys the natural location advantages that some buyers may have held. The effect is to lower the significance of being located close to the seller and increase the significance of other competitive factors, including being located near the market (for uniform delivered pricing and zone pricing systems) and being located near the basing-point. This may have the

effect of unnecessarily increasing transport costs and causing wasteful crosshauling.

A second effect is to distort the competitive relationship between buyers. A uniform pricing system allows all buyers to purchase at an equal price, a zone pricing system places all buyers within a zone on equal footing but magnifies disparities between buyers proximately situated but in different zones, and a basing-point system increases the advantage of those buyers situated near a basing-point.

The competitive impact of delivered pricing systems is unclear. It is worth noting the conclusions in the Attorney General's Report:

Hence "delivered" pricing, as other methods of price quotation, standing alone is wholly equivocal; its business significance derives from the market context in which it appears.

2.4 IMPLICATIONS OF PRICE DISCRIMINATION FOR ECONOMIC WELFARE

(1) Income Distribution Effects.

Price discrimination causes a redistribution of income towards the discriminator and away from the buyer. As no seller has to discriminate, he will only do so if it increases his profits. Third degree price discrimination also redistributes income away from those buyers in the low price elasticity group to those buyers in the high elasticity group. (Buyers in the low price elasticity group usually pay a higher price than under simple monopoly).

Income redistribution does not provide any firm conclusions as to the desirability of price discrimination. Any evaluation of the advantages and disadvantages of redistributing income between groups is subjective and better left to the political arena.


(2) Efficiency Effects.

First, it must be emphasized that price discrimination is symptomatic of monopoly power; the evils of monopoly cannot be attributed to the discrimination. Rather, an evaluation of the efficiency effects of price discrimination turns on whether it causes a more efficient allocation of resources than would occur if the monopolist charged a uniform price.

First and second degree price discrimination almost always raise the level of output nearer to that which would have existed in a competitive market. Hence these two forms lead ceteris paribus to an improved allocation of resources in all but trivial cases.

Third degree price discrimination has more ambiguous effects on efficiency. If demand functions are linear, output is the same as under uniform monopolistic pricing. For third degree price discrimination to increase output above the simple monopoly level, the demand curve in the more elastic market must be less convex from below (i.e. with respect to the quantity axis) than the demand curve in the less elastic market. Scherer notes that there is little evidence that this condition is satisfied more often than not. Thus, the efficiency aspects of third degree are less clear than first or second degree price discrimination.

Posner identifies another cost of monopoly which is aggravated by price discrimination. Posner posits that other sellers will attempt to gain customers from the monopolist by competing in terms other than price. A competing seller would be prepared to offer non-price inducements up to the value of the monopoly profits which he would


30 Scherer, op. cit., p. 259.

receive if he succeeded in gaining the customer, even though the value to the buyer of those inducements is significantly less than the cost of providing them.

Posner describes two situations where this socially wasteful expenditure may occur. First, where the Government (or some other body) fixes the retail price and entry into the market is free, hence there will be many sellers competing for buyers. In the second situation, a seller holds a monopoly position by virtue of barriers to entry to the industry. Here a new entrant may compete in both price and non-price terms. However, established sellers may use non-price competition (such as advertising) to raise further barriers to entry and to secure those monopoly profits available before the new entrant entered the market. Established sellers may also form cartels, lobby government to confer a legal monopoly in the industry, or any other means to limit entry to the market. These actions result in costs which are socially wasteful.

(3) Effects on Competition

Price discrimination may have either pro- or anti-competitive effects in both the seller's and the buyer's market. It can be generally said that systematic price discrimination is anti-competitive while unsystematic price discrimination is pro-competitive.

Price differentials that do not reflect the difference in cost of serving two customers (or supplying two units) may distort the competitive relationships and impair efficiency at the buyer's level.

32 Competition between sellers should force up the value of these non-price inducements to the buyer and hence eliminate some of the social waste incurred. However, the value of the services to the customer will never equal or exceed their cost because in such a case, the services would have been offered in the first place.

33 For sellers to employ monopoly pricing, there must be some barriers to entry which delay the entry of new firms to the industry.

34 Posner assumes that costs incurred to gain or retain a monopoly position have no socially valuable by-products.
These differentials may shield an inefficient buyer from the rigours of competition and allow him to develop and extend a monopoly position for reasons other than efficiency. The 'favour-the-big-ones' is an example of a form of price discrimination that may lead to monopoly. To distort competitive relationships at the buyer's level, the price discrimination must be systematic. An unsystematic discrimination will have no effect on the competitive position of a buyer.

In the same way as a systematic discrimination may affect competitive relationships at the buyer's level, if the discrimination is passed on to buyers of the buyer, then it could also distort relationships at lower levels. Kintner usefully provides some of the distribution structures which may give rise to secondary or tertiary line competitive injury or beyond\textsuperscript{35}.

\textbf{Fig. 2.5 Injury to Secondary Line Competition}

\begin{center}
\begin{tikzpicture}
  \node (M) at (0,0) {M};
  \node (B1) at (-1,-1) {$B_1$};
  \node (B2) at (1,-1) {$B_2$};
  \node (C) at (0,-2) {Customers};

  \draw[->] (M) -- (B1);
  \draw[->] (M) -- (B2);
  \draw[->] (B1) -- (C);
  \draw[->] (B2) -- (C);
\end{tikzpicture}
\end{center}

The manufacturer sells to two buyers who are in competition for common customers. The manufacturer grants one buyer a price discount and this gives him a competitive advantage. If the buyers are not in competition for the same customers, there is no injury. This may occur when either $B_1$ or $B_2$ is a final user of the product.

Fig. 2.6 Injury to Secondary Line Competition: The Dual Distributor

The buyer $B_1$ is a split distributor competing with $B_2$. A differential granted to $B_1$ can injure competition between $B_1$ and $B_2$, and between $B_1$ and $R$.

Fig. 2.7 Injury to Tertiary Line Competition and Beyond

A discount is granted to $W_2$ who passes it on to $R_2$, who then has a competitive advantage over $WR_1$.

Fig. 2.8 Injury to Tertiary Line Competition: Where Secondary-Line Buyers do not Compete
A situation may occur where a discount passed to $W_1$ does not injure competition at the secondary level because $W_1$ and $W_2$ do not compete, however, it is passed on to buyers at lower levels who do compete for the same customers. Therefore tertiary-line injury occurs. It is easy to extend this example to cases where injury occurs at the fourth level.

One case where fourth level injury occurred was *Standard Oil Co. v. Perkins*[^36]. The distribution structure is shown in Fig. 2.9.

**Fig. 2.9 Injury at the Fourth Level**

```
\begin{tikzpicture}
  \node {Standard}
  \child {Signal}
  \child {Hyway}
  \child {Regal}
  \child {Perkins}
  \child {Customers}
\end{tikzpicture}
```

'Kill-the-rival' or predatory pricing is another form of systematic price discrimination which may injure competition, but this time, injury occurs at the seller's level. This situation may also occur where excessive promotional pricing is used.

A second but related case where price discrimination can cause primary line injury is where the seller offers discounts to a large buyer and through these discounts, the seller and buyer become 'tied'. The buyer's custom is effectively denied to other sellers, and this has the effect of foreclosing the market to them. Of course, the price that

[^36]: *Standard Oil Co. v. Perkins*, 396 F.2d 809 (9th Cir. 1967).
the seller offers to the buyer must be low if he is to prevent other
sellers from matching or bettering the price.

Finally price discrimination may have anti-competitive effects
where it is used to support horizontal collusion or to enforce another
trade practice. (However, in these instances, price discrimination is
ancillary to the main problem which should remain the focus of
analysis).

Unsystematic price discrimination may have strong pro-competitive
effects. By varying his price in local markets, a seller may test price
sensitivity. The cost and difficulties of raising or lowering prices
temporarily across-the-board may deter a seller from this action. A
seller may also wish to price according to local demand and supply
conditions prevailing in each market and this may constitute pro-
competitive price discrimination. Thus price discrimination allows
optimum pricing.

A seller may lower price in a market to promote a new product
with the hope of achieving brand-loyalty. To the extent that more
sellers and a greater variety of products means more vigorous rivalry
within the market, this form of promotional pricing is pro-competitive.
The most likely new entrant to a market is a firm who already sells the
product in another market. Thus price discrimination often occurs as a
result of promotional pricing and the pricing of the seller in another
geographic market.

Finally, where the sellers' industry is characterised by rigid
high prices because of an oligopolistic structure, a large buyer may be
able to compel concessions from individual sellers, thereby breaking up
the rigid price structure. The large buyer may compel these discounts by
threats of vertical integration, or switching suppliers. As these
concessions become known to other buyers, they also pressure sellers for
concessions, and the discounts spread, leading eventually to lower
prices throughout the industry. In this way, temporary price discrimination serves to benefit consumers by breaking up oligopolistic pricing structures.

(4) Conclusion.

The previous analysis may seem complicated and no suggestions for price discrimination policy are immediately obvious. As far as price discrimination is indicative of a monopoly position or a monopsonic position, it is the symptom of the problem and not the problem itself.

However, our analysis is limited to identifying anti-competitive market practices. According to Gellhorn, the antitrust laws "seek to maximise consumer welfare by controlling the misuse of private economic power and that they apply where competition is the generally accepted method of social control"\textsuperscript{37}.

In many cases, the discriminator is a public utility or some other body granted a legal monopoly, and justification becomes a matter of politics and not economics. In other cases, the seller or buyer gains and retains his monopoly position by lawful means and he does not impair competition at either the seller's or the buyer's level by the misuse of private economic power. Again, control of such a monopolist does not rest with antitrust law. The concern of antitrust is competition.

Price discrimination that impairs or destroys competition should be prevented, while pro-competitive price discrimination should be encouraged. We conclude that it is desirable to eliminate systematic price discrimination, but encourage unsystematic price discrimination.

CHAPTER III

THE ROBINSON-PATMAN ACT

3.1 INTRODUCTION

The Robinson-Patman Act is the most widely litigated and the most widely criticised piece of anti-price discrimination in the world. The Act has been referred to as "a sacred cow in need of prompt veterinary surgery"\(^1\), and the "Typhoid Mary" of anti-trust\(^2\). Almost every word is subject to intensive debate. A detailed study shows first, the forces that typically motivate price discrimination law; second, the many problems of implementing and applying a price discrimination law; and third, the conceptual deficiencies of price discrimination law. For this reason, a lengthy study of the enactment, implementation and criticism of the Act is contained in Chapters 3 and 4 of this thesis.

3.2 HISTORICAL DEVELOPMENT OF THE U.S. ANTI-PRICE DISCRIMINATION LAW

(1) The Origins of Antitrust.

American anti-trust law is contained in three statutes, the Sherman Anti-trust Act\(^3\), the Federal Trade Commission Act\(^4\), and the Clayton Act\(^5\).


The Sherman Act was enacted in 1890 in response to public reaction to large commercial trusts such as Standard Oil of New Jersey and American Tobacco Co.\(^6\) Section 1 outlaws contracts or combinations in restraint of trade, while Section 2 outlaws attempts to monopolise trade or commerce between states. Enforcement is directed by the Dept. of Justice.

Initially the Act was construed in a restrictive manner by the conservative judiciary\(^7\), however, after these early setbacks, the Act was used successfully in 1904 to attack holding companies\(^8\), and again in 1911 to dissolve the giant Standard Oil Co. of N.J. into approximately 30 smaller companies\(^9\), (although even here the Court warned that only those restraints whose character or effect were unreasonably anti-competitive were outlawed by the Sherman Act).

These cases regenerated the demand for effective anti-trust laws, which had largely run its course by the turn of the century. Both candidates in the 1912 presidential elections included anti-trust stances in their campaigns. The Federal Trade Commission Act and the Clayton Act were enacted by Congress after the victory of Woodrow Wilson in that election.

The Federal Trade Commission Act was enacted in 1914. It established the Federal Trade Commission, a body which was intended to act as a judicial body with greater knowledge in the field of anti-trust, thereby removing many cases from the (then) ineffectual Courts. The sole substantive provision of the Act, Section 5, (as amended in

\(^6\) The Interstate Commerce Commission was established in 1887, also in response to public anger at the tactics of large trusts. This body was intended to assure just and reasonable rates and to prohibit undue discrimination in the railroad industry.

\(^7\) e.g. United States v. E.C. Knight Co., 156 U.S. 1 (1895).

\(^8\) Northern Securities Co. v. U.S., 193 U.S. 197 (1904).

1938 by the Wheeler-Lea Act), prohibits "unfair methods of competition in or affecting commerce, and unfair or deceptive acts or practices in or affecting commerce". Because of its general and all-encompassing nature, this section can be used to reinforce and extend the Sherman and Clayton Acts.

In the same year, the Clayton Act was enacted to compliment the F.T.C. Act. Unlike the Sherman and F.T.C. Acts, this Act attempted to explicitly define and prevent practices that might lead to the growth of monopoly power. Price discrimination was prohibited by Section 2 of this Act. Other practices to be prohibited were exclusive dealing and tying arrangements (§3), corporate mergers (§7) where they injure competition, and interlocking directorships (§8). This Act was to be administered jointly by the F.T.C. and the Dept. of Justice.

The price discrimination provisions were enacted specifically to prevent the classical predatory pricing of the type claimed to have enabled large sellers such as Standard Oil of N.J. to transfer their market power from one market where they held a monopoly to another market where they faced competition.\(^{10}\)

(2) Inadequacy of the Clayton Act.

However, the post-World War I era saw two developments that, in combination, would lead to the enactment of more extensive anti-price discrimination legislation.\(^{11}\) The first development was the depression,\

\(^{10}\) Although see John S. McGee, Predatory Price Cutting: The Standard Oil (N.J.) Case, 1 Jnl. of Law and Economics 137, (1958), who finds little factual evidence or theoretical reason to support this claim.

and the consequent disillusionment with competition that prevailed in the post-depression era of the 1930's. This statement reflects that disillusionment\(^\text{12}\):

The 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.

The second development was a movement towards mass-merchandising and away from the traditional producer-wholesaler-retailer system of distribution. In a Report on the growth of chain stores, the F.T.C. found that the number of operating chain stores increased from 58 in 1900 to 1718 in 1928, this growth occurring significantly at a time of high small business mortality\(^\text{13}\).

Opponents of the chain stores, (chiefly the independent retailers and wholesalers), considered the competitive advantages of the chain stores and mail order houses to be due chiefly to the abusive exercise of their market power to achieve discriminatory concessions from manufacturers. Anti-chain store sentiment was strong, as this statement shows\(^\text{14}\):

The chain-store octopuses, mainly controlled by Wall Street financiers, must be restricted from unfair and discriminatory practices. Since ethics of fair dealing seem unknown to them, these overlords must be prevented by legislation from obtaining special inducements, at the expense of independent dealers, through threats and coercion.

Chain stores were condemned for absentee landlordism, conspiracy with Wall Street, unfair and unethical competition, lack of charity, selling


\(^{13}\) S. Doc. No. 100, 72nd Cong., 1st Sess. 54 (1932).

on Saturdays and Sundays, etc.\textsuperscript{15}

Because Section 2 of the Clayton Act was directed at predatory pricing, it was inadequate to deal with the form of price discrimination caused by abuses of buying power. An unduly restrictive interpretation by the Courts confined the Act to the abuse of selling power and it wasn't until George Van Camp & Sons Co. \textit{v.} American Can Co.\textsuperscript{16} in 1929 that the competition test was extended to cover secondary line injury. Second, the Act was not applicable where the discrimination was accountable to differences in the quantities of goods sold. Third, the meeting competition defence proved an easy defence to charges of price discrimination\textsuperscript{17}.

Congress commissioned a Report on the reasons for the growth of chain stores\textsuperscript{18}. The F.T.C. found that this growth was an expression of consumer demand for the lower prices offered by the chain-stores\textsuperscript{19}. The study revealed that the growth could be explained by lower retail prices, although lower buying prices accounted for only 3 - 35% of these lower selling prices (and some of these lower buying prices may have been cost-justified). The lower selling price resulted chiefly from economies of vertical integration, economies of scale and quantity discounts resulting from the high volume of goods, and lower profit

\textsuperscript{15} See Dept. of Justice Report, \textit{op. cit.}, Chapter 3.


\textsuperscript{17} See, Kintner, \textit{op. cit.}, p. 8; Rowe, \textit{op. cit.}, pp. 6, 7.


\textsuperscript{19} S. Doc. No. 93, 73rd Cong., 2nd Sess. 52 (1934). The study also showed that the use of below-cost sales and 'loss-leaders' was, in fact, less prevalent then previously thought. S. Doc. No. 51, 72nd Cong., 1st Sess. 20 (1932).
margins achieved by a high turn-over\textsuperscript{20}.

The Commission also found that a trend towards final chain store dominance could be expected and that this trend was uncheckable\textsuperscript{21}. It concluded that, in the event of chain store dominance, vigorous competition between chains and independents would provide adequate protection for the consumer\textsuperscript{22}. While some changes to Section 2 of the Clayton Act were recommended, the Commission found this would largely be an ineffective remedy to prevent the demise of the small retailer.

Independent wholesalers and retailers attempted to defend themselves against the encroachment of chain stores and mail order houses by forming co-operative buying groups, or by organising into 'voluntary' chains giving greater bargaining power with manufacturers. Secondary boycotts were employed to compel manufacturers to deal through the 'legitimate' producer-wholesaler-retailer lines of trade. Great effort also went into securing legislative protection.

The National Recovery Administration was established to protect traders from price competition and the deflation that occurred during the depression. This body sought to impose stringent regulation on the distribution process using codes that specified minimum wholesale discounts, condoning group boycotts of manufacturers who sold direct to non-wholesalers, and setting floors on retail prices. This attempt to freeze the traditional channels of distribution was declared unconstitutional in 1935\textsuperscript{23}.

\textsuperscript{20} The F.T.C., itself, concluded that price discrimination was a substantial factor in the lower selling prices of the chains, although statistics gathered by the F.T.C. do not support this conclusion. See the Dept. of Justice Report, pp. 131-132.

\textsuperscript{21} F.T.C. Chain Store Report, pp. 86-87.

\textsuperscript{22} ibid. at p. 19.

The Miller-Tydings Amendment to the Sherman Act was enacted in 1937, and Fair Trading laws were enacted in 44 states between 1933 and 1940, allowing manufacturers to control retail prices through Resale Price Maintenance. Many states also enacted chain-store taxes to discourage the growth of chain stores.24

Within two weeks of the *A.L.A. Schecter Poultry Corp. v. U.S.* decision, the Patman bill (H.R. 8442) was introduced by Representative Patman to the House of Representatives. This was shortly followed by its companion measure, the Robinson bill (S. 3154) introduced to the Senate by Senator Robinson. While the passages of these bills provide interesting reading, it is sufficient for our purposes to present the lessons drawn from that legislative history by the Dept. of Justice in their 1977 Report.

The Report states "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."25 The Report highlights the degree to which sector groups sought to protect themselves and how Congress responded to those demands.

Some examples show how the legislation was moulded by the various sector groups. The Patman bill was drafted by H.B. Teegarden, counsel for the United States Wholesale Grocers Association. The hearing of the House Committee (the Sumners Committee) consisted of a debate between wholesalers and small retailers on one hand, and large retailers and voluntary chains on the other. Manufacturers, agricultural producers, and mass retailers used the hearings on the Borah-VanNuyss bill (S. 4171)

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24 A proposed Federal Chain Store tax was rejected in 1933. This tax was to have increased according to the number of outlets owned by the chain, and the number of states in which the chain operated. Under this tax, A & P would have had to pay $523 m on an annual net income of $9 m.

to voice their opposition to the Robinson-Patman bill. Representative Patman relinquished provisions attacking basing-point pricing systems as the price paid for the cessation of opposition from heavy industry, and the 'for services rendered' clause of the brokerage section was added to appease co-operative buying groups. Similarly, farm groups compelled the deletion of clauses that would have classified their purchasing co-operatives as retailers for the purposes of determining functional discounts.

The second salient feature of the legislative history was the substitution of impressions and anecdotes for solid economic analysis. The Dept. of Justice Report identifies some of the prevalent theories leading to the enactment of the Act.

(i) The assumption that prices should be uniformly higher. Many lawmakers at the time of the Depression attributed the depression to low prices leading to low profits, low wages and employment, and low returns for primary producers. The solution was to increase prices. The Robinson-Patman Act followed in the footsteps of the National Recovery Administration designed to achieve this purpose.

(ii) The assumption that low prices to some buyers were subsidized by increased prices to others. Legislators assumed that to lower prices to some buyers required a compensating increase in prices to other buyers. This particularly pervaded the analysis of predation and discounts granted to large buyers.

(iii) The assumption that discriminatory prices uniformly favour large buyers and never result in lower prices throughout the market. The

26 These groups, seeing that some form of price discrimination legislation was inevitable, supported the more restrictive criminal provisions of the Borah-VanNys bill as an alternative to the wider civil provisions of the Robinson-Patman bill. Ironically, provisions similar to the criminal bill were added to the Robinson-Patman bill.

27 Dept. of Justice Report, op. cit., p. 149.
early theories on price discrimination failed to recognise that price discrimination could lead to lower prices throughout an industry where it was used to break up an oligopolistic pricing structure at the seller's level.

(iv) The assumption that price differentials should primarily, if not exclusively, result from differences in cost. The legislators employed a simplistic idea of pricing, believing it to be based solely on costs.

(v) The assumption that prices are set on the spot and not on a long term basis. The legislators failed to realize that many buyers purchased on long term contracts and therefore their terms of sale were not directly comparable with those buyers who brought at spot prices.

(vi) The assumption that predatory pricing is a prevalent practice of incipient monopolies. A common belief was that monopolies gained and extended their position through the use of predation. This has been disputed28.

The Robinson-Patman Act was enacted on June 19, 1936. Its origins lie, not in the well-founded economic analysis that has come to characterise anti-trust, but rather in "emotional tinged pleas for help and untested economic assumptions"29. However, while its origin may have been in the protection of small business, the Courts have attempted to integrate this Act into the anti-trust structure.

3.3 ADMINISTRATION AND ENFORCEMENT OF THE ROBINSON-PATMAN ACT30

The task of administering and enforcing the Robinson-Patman Act is given to the Federal Trade Commission and the U.S. Dept. of Justice.

28 John McGee, op. cit.

29 Dept. of Justice Report, p. 138.

30 See generally, Rowe, op. cit., Chapter 16.
Of these two, the F.T.C has assumed primary responsibility. Cases may also be brought by the public.

(1) **Enforcement by the F.T.C.**

To ensure compliance with the Act, the F.T.C. has used its powers of consultation and guidance, investigation, hearings and adjudications, and sanctions.

(a) **Consultation and Guidance.** To illuminate the meaning of the obscure text, the F.T.C. has issued official Rules and Guides for compliance, and F.T.C. Commissioners and staff have made policy statements reflecting their views on the law. The Guides are not intended to be a 'legal restatement' of the Act, nor substitute for sound legal advice. They are designed to contribute to the clearer understanding of the Act.

(b) **Investigation.** The F.T.C. is granted broad discretionary powers to investigate a violation of the Act. The existence of such powers has meant that, in most cases, corporate officials have voluntarily complied with F.T.C. requests for information. Failing voluntary compliance, the F.T.C. may visit corporate files\(^{31}\), subpoena testimony or documents\(^{32}\), or demand special reports by corporations. Special reports are reports requested by the F.T.C. providing "answers in writing to specific questions, furnishing to the commission such information as it may require as to the organisation, business, conduct, practices, management, and relation to other corporations, partnerships, and individuals of the respective corporations filing such reports or answers in writing"\(^{33}\).

These broad powers are not unlimited. The right to inspect


\(^{33}\) S. 6(b) Federal Trade Commission Act.
corporate files does not allow the F.T.C. to go on a 'fishing trip',
searching these files "on the possibility that they may disclose
evidence of a crime". Another limitation is that the F.T.C. must
ensure respondent fair and reasonable treatment. Customer and geographic
bounds may be placed on F.T.C. subpoenas, a special report must contain
concise questions and not require subjective answers, etc. The
Commission cannot demand privileged data or unfairly expose the trade
secrets of a business.

(c) Hearings and Adjudications. Formal proceedings are instigated
following the issuance by the F.T.C. of a complaint. At first instance,
the case is adjudicated by a Hearing Examiner, his decision termed the
Initial Decision. This determination may be appealed to the F.T.C. which
acts in both a prosecutorial and judicial capacity. Since 1961, an
Initial Decision is reviewable only on a discretionary basis, removing
the absolute right of Appeal which existed prior to this. The F.T.C.
consists of five Commissioners.

A respondent subject to an Order from a final F.T.C. decision may
petition for review in the federal Court of Appeals, and finally, the
Supreme Court.

(d) Sanctions. Finding a violation of the Act, the Commission may
issue a 'cease and desist' Order requiring the offender to cease the
offending practice. The Order may have wide bounds, applying to sales to
other customers, to other markets, or to similar trade practices.

To avoid the burden and publicity of litigation, a firm charged
with a Robinson-Patman violation may acquiesce by accepting a 'consent
order' to cease and desist without admitting any violation of the law
but waiving all subsequent right to contest the Order's validity.

(2) **Private Enforcement**\(^{36}\)

A private case may be instigated by any member of the public. A successful private case may result in an award for treble damages and the costs of the suit including a reasonable allowance for Attorney's fees\(^{37}\). The rule that a victim may receive thrice the damages sustained by him, is intended to encourage private enforcement and discourage breaches of the antitrust statutes. (An exception to this rule is S. 3 of the Clayton Act containing the criminal provisions of the price discrimination statute. This section has been ruled not an antitrust statute. As such, it may not be enforced by the F.T.C. and plaintiffs in private cases may not receive treble damages)\(^{38}\).

A private litigant must prove that there was injury to his business and that the injury was measureable for the purposes of awarding damages. A violation found by the F.T.C. may be used by a private litigant as evidence that an offence has been committed\(^{39}\).

3.4 **THE STRUCTURE OF THE ROBINSON-PATMAN ACT**

The main prohibition on discriminatory dealing is contained in Section 2 the Clayton Act, as amended by the Robinson-Patman Act\(^{40}\). Seller liability is contained in Section 2(a) which represents the


\(^{37}\) Authorized by Section 4 of the Clayton Act.


\(^{39}\) Section 5 of the Clayton Act.

\(^{40}\) Reprinted in Appendix I. See Rowe, *op. cit.*, Chapter 3 for a comprehensive discussion of the structure of the Act.
main subsection of the section. A plaintiff must first establish the jurisdictional criteria of the Act. The jurisdictional determination turns on these basic statutory requirements:

A discrimination must arise from -

(i) at least two consummated contemporaneous sales transactions,

(ii) by the same seller to different purchasers,

(iii) involving "commodities"

(iv) of "like grade and quality", and

(v) occurring "in commerce".

There is an implicit exemption for sales to government departments.

A prima-facie case is established if the jurisdictional elements are proven and it is shown the discrimination causes injury to competition. Injury occurs where the effect of such discrimination "may be substantially to lessen competition or tend to create a monopoly in any line of commerce", or may be "to injure, destroy, or prevent competition"

(i) with the grantor of the discrimination, (primary-line injury); or

(ii) with a "knowing" beneficiary of the discrimination, (secondary line injury); or

(iii) with customers of either of them, (secondary and tertiary-line injury).

A respondent may justify a prima-facie illegal discrimination by showing -

(i) that the price differential reflects the cost savings attributed to supplying goods to a particular purchaser, or

(ii) that the challenged differential was in response to changing market conditions affecting the market for, or the marketability of, the goods concerned, or

(iii) that the lower price was made in good faith to meet an
equally low price of a competitor.

There is a fourth implicit defence if the goods are "available" to the disfavoured buyer.

Although the Robinson-Patman Act was enacted to prevent buyers from abusing their market power, the major provisions of the Act focus on the seller. Section 2(f), however, declares it unlawful for buyers "knowingly to induce or receive a discrimination in price" prohibited by the Act.

The Act contains three prohibitions on indirect price discrimination. These are known as the per se provisions as they do not require a showing of competitive impact and do not allow a cost justification defence. Section 2(c) prohibits the granting or receiving of brokerage or equivalent payment, "except for services rendered". Sections 2 (d) and (e) prevent the payment or granting of promotional allowances, services or facilities except on proportionally equal terms to all buyers. Sections 2 (d) and (e) allow a 'meeting competition' defence.

Finally Section 3 of the Robinson-Patman Act contains criminal prohibitions against price discrimination.

3.5 REQUIREMENT OF CONSUMMATED CONTEMPORANEOUS SALES

For a discrimination to occur, there must be at least two consummated contemporaneous sales. This requirement precludes the Act's application to 1) refusals to deal, 2) consignment or non-sale arrangements, and 3) noncontemporaneous transactions.

(1) Refusals to Deal, Executory Contracts, and Offers to Sell.

As the Act requires two consummated sales, a refusal to deal cannot constitute a Robinson-Patman violation. Section 2(a) of the Act
states 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".
Thus the Act allows the seller to select the customers, or classes of
customer, with whom he deals.

Rowe notes that this is essentially a truism which adds nothing
to the prohibitions as the Act presupposes two completed transactions
on different terms\textsuperscript{41}. (For example, the Third Circuit in \textit{Shaw's, Inc. v. Wilson-Jones Co.} found a discrimination in price must occur "between
different purchasers" and must therefore require at least two completed
purchases to have taken place)\textsuperscript{42}.

This requirement codifies the Supreme Court ruling in \textit{U.S. v.
Colgate Co.}, which upheld the right of a seller to select his own
customers provided the refusal to sell was not ancilliary to the
achievement of some other unlawful marketing objective\textsuperscript{43}.

One exception to this requirement is where the supplier continues
to tender goods to a disgruntled customer rather then simply refusing to
deal. The Fifth Circuit held the customer need not have gone through
with the formality of purchase at the discriminatory higher price "in
order to attain the status as a competing purchaser under the Act, as
its failure to do so was directly attributable to the defendant's own
discriminatory practice"\textsuperscript{44}. It seems, however, that the Court may have
been persuaded by the long-established business relationship between the
seller and the buyer. Usually an offer to sell will not be sufficient to

\textsuperscript{41} Rowe, \textit{op. cit.}, p. 46.

\textsuperscript{42} Shaw's, Inc. v. Wilson-Jones Co., 105 F.2d 331 (3d Cir. 1939).

\textsuperscript{43} United States v. Colgate & Co., 250 U.S. 300 (1919).

\textsuperscript{44} Bruce's Juices, Inc. v. American Can Co., 187 F.2d 919, 924
(5th Cir. 1951), 190 F.2d 73, 74 (5th Cir. 1951).
establish a charge of price discrimination\textsuperscript{45}.

In another case the Court accepted an unexecuted contract as a sale. In \textit{Aluminum Co. of America v. Tandet} the Court accepted an enforceable executory contract as sufficient to establish one leg of a discriminatory transaction\textsuperscript{46}. The Court considered the incidence of delivery and payment would affect only the type and kind of remedies available to the plaintiff, but in no way was their legal status as seller and buyer diluted. This differed from an earlier ruling in \textit{A. J. Goodman & Sons, Inc. v. United Lacquer Mfg. Corp.}, although in that case the sale was contingent on acceptance of the plaintiff's bid by the State of New Hampshire\textsuperscript{47}. The presence of an enforceable contract was the crucial distinguishing factor in the later case.

\section*{(2) The 'Sale' Requirement.}

The 'sale' requirement removes a growing number and variety of non-sale transactions from the coverage of the Act. These non-sale transactions include consignment and agency agreements, credit transactions, leases, gifts, and membership rights. Exclusion of these non-sale transactions allows greater pricing flexibility in these areas.

Ironically, in \textit{Ace Books Co.}\textsuperscript{48} the use of an agency agreement extended the publisher's liability to include retailers who were customers of the wholesaler agent even though the publisher, at no time, dealt directly with those retailers.


(3) Non-contemporaneous Sales Transactions.\footnote{49} Non-contemporaneous sales are exempt from the coverage of the Act, thereby allowing for variations in price that result from changing market conditions. The time lag between the first and second sales for the two sales to be noncontemporaneous will differ depending on the character of the good and the volitility of the market.

Similarly a seller's spot and future price quotations can differ freely, although competing purchasers should be subject to the same conditions of ordering. In \textit{Corn Products Refining Co. v. F.T.C.}\footnote{50} the Supreme Court upheld an F.T.C. Order invalidating the practice by glucose suppliers of permitting some customers to book orders at old prices for only five days after an announced price rise, while granting the same option to other buyers for more extended periods.

3.6 THE SALES MUST BE MADE BY THE SAME SELLER TO DIFFERENT PURCHASERS

To obtain jurisdiction there must be a discrimination in price attributable to the same seller in dealing with different purchasers. This raises three questions:

(a) Whether sales by a parent and a subsidiary are made by the same seller;

(b) Whether a subsidiary can be a 'purchaser' within the meaning of the Act; and

(c) Whether a purchaser must buy direct from the seller;

(1) \textbf{Whether Sales by a Parent and its Subsidiary are made by the 'Same Seller'.}

Generally the Courts have held that sales made by a parent

\footnote{49} See also the Changing Conditions defence, \textit{infra}, p. 151.

\footnote{50} \textit{Corn Products Refining Co. v. F.T.C.}, 324 U.S. 726 (1945).
corporation and by its subsidiary are sales made by two different sellers unless there is evidence that the parent directs or participates in the pricing decisions of the subsidiary. In Baim & Blank, Inc. v. Philco Corp.\textsuperscript{51}, sales by a supplier, Philco Corporation, and by its wholly-owned subsidiary, Philco Distributors, Inc., were deemed not made by the same seller and therefore not subject to review under the Robinson-Patman Act. Evidence that the subsidiary was wholly-owned by the parent and that its officers, with one exception, were also officers of the parent corporation failed to persuade the Court that the subsidiary was sufficiently controlled by the parent to subject the parent corporation to liability.

In National Lead Co. v. F.T.C.\textsuperscript{52}, the Seventh Circuit required that there be "such complete control of the subsidiary by the parent as to render the former a mere tool of the latter, and to compel the conclusion that the corporate identity of the subsidiary is a mere fiction".

(2) Whether a Subsidiary can be a 'Purchaser' within the meaning of the Act.

Treating a subsidiary as independent of the parent company can have its difficulties also. Sales by the parent to the wholly-owned subsidiary may need to be at comparable prices to sales made to independent competitors of the subsidiary, otherwise a sale to the wholly-owned 'purchaser' may form one half of a discriminatory transaction. This 'bath-tub' theory was applied to a Robinson-Patman situation in Danko v. Shell Oil Co., where the Court declined to dismiss a complaint alleging that Shell had discriminated in price in favour of


\textsuperscript{52} National Lead Co. v. F.T.C., 227 F.2d 825 (7th Cir. 1955), rev'd on other grounds 352 U.S. 419 (1957).
its wholly-owned service stations. The Court rejected the theory advanced by Shell that for anti-trust purposes, the definition of purchaser, customer, and distributor are a matter of competitive substance and competitive function and not of form\textsuperscript{53}.

However, this case has been distinguished and severely limited by the same Court. It seems that the Courts will be reluctant to treat intra-company transfers as arms-length sales although there is some inconsistency with the practice of not attributing sales of a controlled subsidiary to the parent company. Those cases that have treated transfers as sales usually feature an unusual degree of purchasing autonomy by the subsidiary, or a competitive relationship between the subsidiary and the independent customer.

(3) Whether a purchaser need buy direct from a manufacturer.

Sales by an independent distributor will not normally be attributed to the original supplier, but again an exception may occur where the supplier has substantial control over the activities of the distributor. The F.T.C. has developed the "Indirect purchaser" doctrine which treats the customers of the distributor as customers of the original supplier. This doctrine may be applied where the autonomy of the distributor has been supplanted by the supplier, who fixes the resale price, selects customers, and takes an active interest in the redistribution of the goods.

In Kraft-Phenix Cheese Corp.,\textsuperscript{54} retailers were classed as "indirect purchasers" of the respondent, who, "by personally soliciting them and making effective its price policies and schedules as applied to them", had taken over the normal responsibility of its intermediate


\textsuperscript{54} Kraft-Phenix Cheese Corp., 25 F.T.C. 537, 546 (1937).
distributor organisation. In *Whitaker Cable Corp.*\(^{55}\), the Commission viewed as "indirect purchasers" those customers of the supplier's distributors who signed contracts with him and depended on his approval, since the supplier's degree of control exercised over sales to these accounts "was such that the sales were in all essential respects sales made by the respondent".

An extreme application of this doctrine occurred in *Purolator Products, Inc.*\(^{56}\) Purolator used a complex distribution system, part of which is shown in Fig. 3.1.

**Fig. 3.1 The Distribution System of Purolator Products, Inc.**

Purolator sold filters exclusively to warehouse distributors at prices:

(i) 32c if filters resold to Independent Jobbers,

(ii) 30.4c if filters resold to Affiliated Jobbers who resold to Independent Jobbers,

(iii) 36.4c if filters resold to Affiliated Jobbers who resold to Dealers,

(iv) 38c if filters resold to Dealers.

Purolator also suggested 40c as the appropriate price which

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warehouse distributors and affiliated jobbers should sell to independent jobbers. The graduated prices and suggested resale prices were intended to reward each level of distribution for services performed. The F.T.C. found that:

(i) Purolator's contact with jobbers allowed them to be treated as 'indirect purchasers' from Purolator, thus meeting the 'same seller' requirement.

(ii) As such, independent jobbers brought filters at 40c whereas warehouse distributors brought filters for resale to dealers at 38c. Both groups were in competition for the dealers and this price differential injured competition between them.

The F.T.C. completely disregarded any evidence that showed that warehouse distributors may have performed valuable services which warranted the extra discount that they received.

3.7 THE REQUIREMENT OF COMMODITIES

The Robinson-Patman Act is further confined to sales of goods and does not extend to services and intangibles. Generally a restrictive reading of "commodities" has been adopted. This seems consistent with the legislative history of the Act where Congress was concerned with the supply of tangibles through grocery chains and mail-order houses, and with the text of the Act which requires goods to be of "like grade and quality", allows for differentials that reflect differences in the cost of "manufacture, sale, or delivery", and exempts price changes which result from the changing "marketability of the goods".

Sales which include both physical elements and intangible factors or services, where the intangible portion is dominant, are also exempt from the coverage of the Act. The Sixth Circuit in General Shale Products Corp. v. Struck Construction Co., would not apply the Act to
quotations of brick plus other materials and work as the bid "was not divisible into a contract for work and labour, and a contract for the sale of brick"57.

   Distinguishing between tangible goods, and intangibles and services is difficult. Newspaper advertising provides one example of the perplexing problems that may arise. In *Times-Mirror Co.*, the F.T.C. concluded that the legislative history of the Act is ambiguous, and that "commodities" should therefore be construed in light of the objectives of the statute rather then attempting to distinguish between tangibles and intangibles58. It found that advertising space was covered since it is relatively fungible and discrimination in its price can be just as injurious as discrimination associated with the purchase or resale of goods59.

3.8 THE MEANING OF 'LIKE GRADE AND QUALITY'

(1) History and Purpose of the 'Like Grade and Quality' Test.

    The Act focuses on discrimination between purchasers buying goods of 'like grade and quality'. In the original Clayton Act the seller could defend a prima-facie case of price discrimination by showing that


59 This differs from an early informal ruling of the F.T.C. that exempted advertising space sales, on the principle that what is sold is, by nature, a service (i.e. the readership circulation) and the printed paper is merely a vehicle to convey this service. Cases involving TV broadcasting time have been dismissed by the Courts. Amana Refrigeration Inc v. Colombia Broadcasting System, N.D. Ill. No.57 C1177, Feb 17, 1959, aff'd, 295 F.2d 375,378 (7th Cir. 1961), cert. denied, 369 U.S. 812 (1962). However, the Supreme Court, in reference to the Government's concession that advertising space was not a "commodity" under S3 of the Clayton Act, commented "We express no view on that statutory interpretation". Times-Picayune Publishing Co. v. U.S., 345 U.S. 594 609-610 n. 27 (1953).
the goods were made "on account of differences in the grade, quality, or quantity of the commodity sold", thus "differences in quality" was a defence to a charge of price discrimination. The Robinson-Patman Act requires a showing of 'like grade and quality' before a prima-facie case can be established.

The Attorney General's Committee saw the test as designed to limit the instances where the Act may be invoked in order to prevent the Act being used as a type of price control legislation for goods that are only roughly comparable: 60

The 'like grade and quality' concept, we think was designed to serve as one of the necessary rough guides for separating out those commercial transactions insufficiently comparable for price regulation by the state.

Many products supplied by a manufacturer may be considered homogeneous and therefore of 'like grade and quality'. Problems arise where there is some product differentiation or where the same goods (physically) are sold under different brand-names.

(2) Product Differentiation

Where products are physically similar but not identical, the Courts have enquired whether the differences are actual or merely cosmetic changes. The Attorney General's Committee states that: 61

Actual and genuine physical differentiations between two different products adapted to several buyers' uses, and not merely a decorative or fanciful feature probably remove differential pricing of the two from the reach of the Robinson-Patman Act.

This test of determining 'like grade and quality' according to physical similarity has created problems and a further test of functional interchangeability was used in Bruce's Juices, Inc. v. American Can Co. Here the plaintiff was supplied 3.14 inch cans at a

60 Attorney General's Report, p. 156.
61 ibid, at p. 158.
higher price than that paid by purchasers who brought 3.12 inch cans. The Court found the cans to be of 'like grade and quality' as they:

...gave substantially identical performance ... all of the cans were adapted for the function for which they were sold and purchased, to wit, as containers of juice, and they were "the same kind of goods".

However the functional interchangeability test was rejected in Atalanta Trading Corp. v. F.T.C. Here the F.T.C. considered "ham is ham", and condemned price differences relating to the sale of hams of varying sizes, pork shoulders, loin rolls, and Canadian bacon. The Second Circuit reversed, arguing that the import of cross elasticity of demand into the 'like grade and quality' test allowed the comparison of unlike transactions and expanded the law to an unacceptable point.

Two further cases provide examples of the functional interchangeability test and show the movement to a test of 'commercial fungibility'. In Universal-Rundle Corp., substantial physical differences in design that had no functional import but commanded preference among consumers, were held by the Commission to distinguish the goods under the 'like grade and quality' test. However, in Joseph Kaplan & Sons, Inc., design but not functional differences were held insufficient to distinguish shower curtains. The crucial factor in Universal-Rundle Corp. appears to have been the demonstratable consumer preference shown for the design differences.

These decisions herald a test of 'commercial fungibility'. Products would be deemed 'fungible' "if the business community would as

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63 Atalanta Trading Corp. v. F.T.C., 258 F.2d 365 (2nd Cir. 1958).

64 Universal-Rundle Corp., 65 F.T.C. 924, rev'd on other grounds, 352 F.2d 831 (7th Cir. 1695), rev'd, 387 U.S. 244 (1967).

lief take the one for the other for the same amount of money". The goods must, of course, also be of 'like grade and quality'. Rowe notes that "as for distinctions in size or design, the custom of the trade might provide the clue. If the dimension of cans is of the commercial essence to canners, even a minor disparity in measurement would disprove 'commercial fungibility'".

This test was applied in **Fred Meyer, Inc. v. F.T.C.** where the Court found that peaches were of 'commercial identity or fungibility' despite arguments that the quality of canned peaches varied according to time and place of packing. In **Checker Motors Corp. v. Chrysler Corp.**, the Court, when comparing taxi-cabs and passenger automobiles, said:

> ...Cross-elasticity of demand, substitutionability, physical appearance, and identity of performance are factors to be considered... Although it seems clear that denominating one vehicle a "taxicab" and an identical one a "passenger car" will not preclude a finding of 'like grade and quality' ....if there are substantial physical differences in products affecting consumer use, preference, or marketability, such products are not of 'like grade and quality', regardless of manufacturing costs.

**(3) Brand Differentiation**

Branded goods provide another significant problem for the Courts. Branded goods may command a higher price because they have superior acceptance over physically identical private label goods. The enhanced value may result from advertising, use of reputable trade marks, etc. The concept of brand names commanding a price distinct from the product is upheld in our patent laws.

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66 Rowe, *op. cit.*, at pp. 74, 75.

67 *ibid*, at p. 76.


69 **Checker Motor Corp. v. Chrysler Corp.**, 132 F.2d 425, 428 (5th Cir. 1942), *cert. denied* 318 U.S. 780 (1943).
A branded good would not be considered of 'like grade and quality' as a private label good by an economist because of the premium created by the brand label. The F.T.C., however, has consistently held that brand labels may be disregarded when determining 'like grade and quality' and that economic factors inherent in brand names should be considered in the 'injury to competition' and cost justification provisions.

The most important case dealing with branded goods is **F.T.C. v. Borden Co.**\(^{70}\). Here Borden marketed physically identical milk through two different brand names. The **Borden** brand label commanded a significantly higher price that the private label of the retail outlet to whom Borden supplied. Borden's price to this buyer was lower than its price to other buyers reflecting the lower consumer preference for the private label good. The Supreme Court explicitly rejected any argument that 'grade' equated with economic factors such as brand names and found that physically identical goods are of 'like grade and quality' even where one brand commands a higher price. This ruling adopts the recommendation of the Attorney General's Report that economic factors should be considered in the 'injury to competition' and cost justification provisions of the Act\(^{71}\).

A refusal to apply the 'commercial fungibility' test to branded goods represents an inconsistency in the Court's position. However, application of the test to branded goods would deny the protection of the Act to buyers of goods even if the consumer preference was negligible. This may encourage price differentials far in excess of those justified by the consumer preference\(^{72}\).

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\(^{71}\) Attorney General's Report, pp. 157-158.

\(^{72}\) See infra, p. 223.
3.9 THE COMMERCE REQUIREMENT

The Federal Anti-trust laws are limited by the power of Congress to regulate inter-state commerce. Consequently the Robinson-Patman Act applies only to inter-state commerce and international business arrangements, although the former is the main priority of the enforcement agencies.

(1) The 'Commerce' Requirement

The Robinson-Patman Act requires that the discriminator be "engaged in commerce", that the challenged discrimination occur "in the course of such commerce", and that "either or any of the purchases involved in such discrimination are in commerce". This falls short of the wide "affecting commerce" doctrine applied in Sherman Act and F.T.C. Act cases.\(^3\)

The first two "commerce" requirements are subsidiary to the third, which requires the sales to be "in commerce". If this is proven, then, ipso facto, the discriminator is "engaged in commerce" and the challenged discrimination has occurred "in the course of such commerce". This means the plaintiff must show that at least one of the discriminatory transactions must cross a state line, although it doesn't matter whether it is the lower or higher priced transaction.

While the "commerce" requirement is more restrictive then that used by the Sherman Act, the 'flow of commerce' doctrine has been used to widen the scope of the Robinson-Patman Act. In the Standard Oil Co.

\(^3\) For example, in U.S. v. Employing Plasterers Assn., 347 U.S. 186 (1954) the Court applied the 'affecting commerce' doctrine to uphold a complaint concerning restraints on plastering work in the Chicago area, because they could adversely affect the otherwise continuing flow of plastering materials from out-of-state origins to Illinois job sites. The Supreme Court rejected the 'affecting commerce' standard in Robinson-Patman Act cases in Gulf Oil Corp. v. Copp Paving Co., 419 U.S. (1974).
v. F.T.C. decision, the Court ruled that local warehouses and facilities used to redistribute goods that originated from across a state line were part of a larger inter-state movement and thus subject to Robinson-Patman jurisdiction. This ruling however, applies only where the goods are produced in one state and sold in another. Price quotations for goods produced and sold in the same state remain exempt under the Act.

Rejection of the wider "affecting commerce" test in favour of the "in commerce" test limits the scope of the Robinson-Patman Act and, in instances where the discriminatory sales are made intra-state, denies the protection of the Act to disfavoured firms. Robinson-Patman liability may be minimised where franchised distributors or bona-fide independent subsidiaries are employed to distribute goods across state lines.

(2) Export Arrangements

Export arrangements are exempted as the Act applies only to goods "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". While this restriction applies only to Section 2(a), cases involving exports brought under Sections 2(c), (d) and (e) would probably be exempted to remain consistent with Congressional intent.

(3) Import Arrangements

Import arrangements are not exempted although comity and difficulties with international litigation may limit the application of the Act. Nevertheless, the Dept. of Justice obtained a consent decree from French and German potash producers in 1927, preventing them from "discriminating, directly or indirectly, between purchasers, dealers, or

customers, of potash salts located within the United States" unless justified under one of the statutory provisos. As the Robinson-Patman Act retains the import trade jurisdiction of the original Clayton Act, these decrees provide a precedent for applying the Act to other import arrangements.

3.10 EXEMPTION OF SALES TO THE GOVERNMENT

Sales to the Federal government are exempted from the coverage of the Act. A memorandum submitted to the House Judiciary Committee by H. B. Teegarten, the bill's draftsman, explains: "The answer is found in the principle of statutory construction that a statute will not be construed to limit or restrict in any way the rights, perogatives, or privileges of the sovereign unless it so expressly provides - a principle inherited by American jurisprudence from common law". It seems also that State governments will receive similar treatment to the Federal government.

3.11 THE MEANING OF "TO DISCRIMINATE IN PRICE"

Having established the jurisdictional elements of two consummated contemporaneous sales made by the same seller to different purchasers of commodities of like grade and quality occurring in commerce, the plaintiff must show there has been a discrimination (either direct or indirect) in the price.

75 U.S. v. Deutsches Kalisyndikat Gesellschaft, 2 Decrees and Judgements in Civil Federal Anti-trust cases 1333 (S.D.N.Y. 1929).
76 Hearings Before the House Committee on the Judiciary on Bills to Amend the Clayton Act, 74th Cong., 1st Sess. 250 (1935).
(1) The Meaning of 'Discrimination'

The legal concept of price discrimination differs from the economic concept which states that a discrimination in price has occurred if the ratio of price to cost differs between two sales. As Blakeney points out, the two concepts must differ as the economic concept requires no presumption about costs, while the legal concept assumes costs (and hence prices) are equal and then provides a defence for those cases where the costs differ.

This leads us to the legal meaning of 'discrimination in price'. A discrimination in price is synonymous with a difference in price. For the purpose of establishing a **prima-facie** violation the costs of supplying each buyer are presumed to be equal and therefore the prices charged to each are also presumed to be equal. The Supreme Court in their authoritative **F.T.C. v. Anheuser-Busch, Inc.** decision, said:

> We are convinced that...there are no overtones of business buccaneering in the S2(a) phrase 'discriminate in price'. Rather, a price discrimination within the meaning of that provision is merely a price difference. ...[T]he statute itself spells out the conditions which make a price difference illegal or legal, and we would derange this integrated statutory scheme were we to read other conditions into the law by means of the nondirective phrase "discriminate in price".

The Court rejected the comment of Representative Utterbuck, made to the House of Representatives, who said:

> In its meaning as simple English, a discrimination is more than a mere difference. Underlying the meaning of the word is the idea that some relationship exists between the parties to the discrimination which entitles them to equal treatment, whereby the difference granted to one casts some burden or disadvantage upon the other. If the two are competing in the resale of the goods

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79 Supra, p. 13, 14.


82 80 Cong. Rec. 9416 (1936).
concerned, that relationship exists. Where, also, the price to one is so low as to involve a sacrifice of some part of the seller's necessary costs and profit as applied to that business, it leaves that deficiency inevitably to be made up in higher prices to his other customers; and there, too, a relationship may exist upon which to base the charge of discrimination. But where no such relationship exists, where the goods are sold in different markets and the conditions affecting those markets set different price levels for them, the sale to different customers at those different prices would not constitute a discrimination within the meaning of this bill.

The Supreme Court ruling adopts a simple rule-of-thumb and relegates examination of a relationship between buyers and of the business buccaneering of the seller to the injury to competition, cost justification, and meeting competition provisions of the Act.

(2) The Meaning of 'Price'.

Price is defined as the actual invoice price quotation by a seller, 1) inclusive of any elements of prepaid freight, 2) less any discounts or offsets against the invoice price.\(^{83}\)

This definition has evolved from F.T.C. attacks on various pricing systems, notably delivered pricing systems. F.T.C. attempts to attack delivered pricing systems have stumbled on the threshold difficulty of establishing a discrimination in price. Initially a particular concept of price, the net-mill price, was used. This price is the net price received by the seller after deducting all freight costs incurred. Where freight absorption and phantom freight occur the net-mill price will differ between buyers.

The attack on delivered pricing reached its apex in 1948 when the Cement Institute case came before the Supreme Court.\(^{84}\) The issue was a multiple basing-point system collusively adopted by cement suppliers on an industry-wide basis. The Court condemned this scheme and gave dicta

\(^{83}\) Rowe, op. cit., p. 87.

\(^{84}\) Cement Institute, 333 U.S. 683, 722-725 (1948).
approving the definition of price as the net-mill price. The dicta however seems limited to situations where collusion is present, and has not been adopted in cases involving basing-point systems adopted by individual firms. In *F.T.C. v. A. E. Staley Mfg. Co.*\(^{85}\) and *Corn Products Refining Co. v. F.T.C.*\(^{86}\), two cases involving the use of Chicago as a basing point for the sale of glucose, the Supreme Court focussed on delivered price.

The F.T.C. abandoned the net-mill definition in the early 1950's and focussed on the price paid by the buyer. In 1953 in *National Lead Co.* and *Chain Institute, Inc.*, the F.T.C. dismissed cases involving multiple basing point and zone delivered systems and affirmed the buyers net price as the appropriate definition of price\(^{87}\). This is consistent with the legislative intent, Congress having rejected an amendment to the original bill to define price as the amount received by the vendor less any transportation costs\(^{88}\). The Attorney General's Committee concurs with this approach, saying\(^{89}\):

> Since the paramount legal inquiry of the Robinson-Patman Act centers on the "injurious" handicaps imposed by discriminations on "disfavored" customers, it is this "actual price" paid by buyers which determines their competitive standing vis-a-vis each other, and hence must be the significant index of legality.

Price is net of any discounts which the buyer is entitled to receive, allowing the courts to examine transactions even where the

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\(^{86}\) *Corn Products Refining Co. v. F.T.C.*, 324 U.S. 726 (1945).

\(^{87}\) *National Lead Co.*, 49 F.T.C. 791 (1953); *Chain Institute, Inc.*, 49 F.T.C. 1041 (1953).

\(^{88}\) The pertinent provisions are contained in the Utterback bill [H.R.10486, 74th Cong., 2d Sess. (Jan. 22, 1936)], which read 'The word 'price', as used in this Section 2, shall be construed to mean the amount received by the vendor for each commodity unit, after deducting actual freight or cost of other transportation, if any, allowed or defrayed by the vendor'.

\(^{89}\) Attorney General's Report, p. 217.
invoice price is non-discriminatory between buyers. The F.T.C. Advisory Committee on Cost Justification rationalises this view:

In general, the price of a service or commodity is measured by the value of the consideration which passes from the buyer to the seller in the exchange: it is the amount which the buyer agrees to pay and the seller agrees to take... The price, in any instance, is net of all applicable allowances, discounts, and rebates which buyer receives or is entitled to receive in view of the quantities and methods of his purchases.

The F.T.C.'s decision in Firestone Tyre & Rubber Co. reflects this view. The resulting order forbade discriminations in "net prices", broadly defined as taking "into account rebates, allowances, commission, discounts, terms and conditions of sale, and other forms of direct or indirect price reductions, by which net prices are affected".

The Anheuser Busch definition of price precludes the Act's application to uniform delivered pricing systems. As the Supreme Court noted in Staley, the law tolerates "a uniform delivered price at all points of delivery, for in that event there is no discrimination in price". In fact, the equation of price differentiation with price difference precludes the application of the law to any one-price system. A seller is not compelled to grant functional discounts, cost justified discounts, etc, to buyers even where the costs of serving two buyers differs.

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92 55 F.T.C. at 1764.


94 In Bird & Son, the F.T.C. approved a supplier's policy of quoting a single uniform price to large retailers and to jobbers. 25 F.T.C. 548, 553 (1937). In Klein v. Lionel, a case with similar facts, (fn. continued p. 74).
(3) 'Indirect' Price Discrimination

The jurisdiction of the Act is extended by the inclusion of 'indirect' price discrimination. Conditions of sale and terms of trade incidental to the main sales contract which affect how much the buyer actually receives for the contract price are all subject to the proscriptions of the Act. Examples of such incidental terms include delivery terms, free goods or bonus merchandise, sales return privileges, guarantees against price declines, discounts for cash payments, and warehouse services.95

The meaning of 'indirect price discrimination' was considered by the Supreme Court in Corn Products Refining Co. v. F.T.C.96. There, the Court condemned as indirect price discrimination favourable booking arrangements allowing buyers to book goods in advance at current prices granted to some buyers for thirty days and to others for only five days. Kintner notes "...any discrimination supporting a finding of a resulting reduction in prices to some competitors over others will constitute an indirect discrimination. The test is the result, not the appearance"97. Bona-fide, separate, independent business arrangements between a supplier and a customer that have no connection with a sales contract will not be considered indirect price discriminations. For example, the F.T.C. in General Foods Corp. declined to find payments to some customers in return for the performance of storage and delivery services discriminatory, saying "in the absence of some showing that they are grossly in excess of the cost or value of the services rendered, it

95 See Kintner, op. cit., pp. 65-66.
96 Corn Products Refining Co. v. F.T.C., 324 U.S. 726 (1945).
97 Kintner, op. cit., p. 66.
cannot be found that they constitute any sort of a rebate or price reduction on other merchandise bought by the [customer] from the respondent for resale."\(^{98}\)

The F.T.C. and Courts have had particular difficulty distinguishing between indirect discriminations attacked under S. 2(a) and payments of brokerage and the disproportionate granting of promotional services and allowances attacked under Sections 2(c), 2(d) and 2(e). The distinction is important because of the 'per se' nature of the latter forms of indirect discrimination, and the F.T.C. has an incentive to bring cases under those sections.\(^{99}\)

3.12 THE INJURY TO COMPETITION TEST

(1) **Introduction**

After establishing jurisdiction, the plaintiff must show that the discrimination has caused competitive injury. The discrimination is proscribed where its 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'. (This proscription is, of course, subject to the defences provided in the Act).

The competitive injury clause used in the Robinson-Patman Act is more extensive than that which is used in the Sherman Act, although this still represents a compromise from the original Patman proposals which condemned all discrimination irrespective of their impact on

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\(^{99}\) This problem is discussed in the Brokerage section, infra, pp. 185, and the Promotional Allowances and Services section, infra, pp. 199.
competition\textsuperscript{100}.

The term 'may be substantially to lessen competition or tend to create a monopoly in any line of commerce' was adopted from the original Clayton Act\textsuperscript{101} and is generally consistent with the language of other anti-trust statutes. The second competitive injury test, 'or to injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or the customers of either of them' was introduced in the 1936 amendment. This addition makes explicit the ruling in \textit{George van Camp \& Sons Co. v. American Can Co.}\textsuperscript{102} and allows the Courts to examine the effect of the discrimination on primary, secondary, and tertiary line competition.

The difference between the two competitive injury clauses is made clear by this statement from Senator Utterbuck\textsuperscript{103}:

\begin{quote}
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 field. Competition in the local field has not been lessened, since one competitor has been replaced by another; but competition with the grantor of the discrimination has been destroyed.
\end{quote}

\begin{quote}
Justification for this extension of the competitive injury clause can be found in the Senate Report on the Robinson-Patman Act which
\end{quote}

\textsuperscript{100} The Patman bill, HR 8442, banned 'discriminations' in price or terms of sale in interstate commerce, regardless of their competitive impact. (Exceptions were provided for cost-justified discounts and functional discounts). The Committee hearings on the bill identified two flaws. First, it was doubtful that a law prohibiting non-injurious price differentials would be constitutional. Second, it was feared the Act might be interpreted to apply only to cases where buyers were in competitive contact, and therefore would not reach territorial price discrimination.

\textsuperscript{101} The 1914 Clayton Act prohibited a discrimination "where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce".

\textsuperscript{102} See supra, p. 45 n. 16 and accompanying text.

\textsuperscript{103} 80 Cong. Rec. 9417 (1936).
viewed the "injury" clause in S. 2 of the old Act as having:

...in practice been too restrictive, in requiring a showing of general injury to competitive conditions in the line of commerce concerned, whereas the more immediately important concern is an injury to the competitor victimized by the discrimination. Only through such injuries, in fact, can the larger general injury result, and to catch the weed in the seed will keep it from coming to flower.

The amendment introduces the incipiency doctrine to the competitive injury clause.

(2) Forms of Competitive Injury

While the Act condemns discriminations whose effect may be substantially to 1) lessen competition, 2) tend to create a monopoly in any line of commerce, or 3) injure, destroy, or prevent competition with any person who either grants or knowingly receives the benefit of such discrimination, or the customers of either of them, in practice these types of competitive injury have not been considered separately. First, the term 'substantially' has been applied to modify all three types of injury with the effect of minimising the distinction between them. Second, the few attempts to distinguish between the types of injury have not met with judicial acceptance. Rowe writes:

Fundamentally, the statutory distinctions have not been meaningful in practice since only test (3) concerning harm to competition with grantors or recipients of discriminations has been important in price discrimination cases. The effect of a pricing practice should normally register on competition with individual firms long before its impact is felt over an entire "line of commerce" or is instrumental in building "monopoly". Inasmuch as a demonstration of competitive effects under any one of the alternative tests gives rise to a prima-facie violation, no incentive exists to extend the inquiry and proof beyond this least exacting criterion.


105 See Rowe, op. cit., pp. 125, 126.

106 Rowe, op. cit., p. 126, (emphasis supplied, footnote omitted).
(3) **Competition v. Competitors**

The statutory injury test focuses upon injury to individual competitive relationships and suggests that the Act is concerned with the plight of competitors as well as competition. Clearly this was the intention of Congress\(^{107}\):

Unlike a "pure" Robinson-Patman, concerned only with the preservation of competition, the real Robinson-Patman Act is explicitly directed towards 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.

However, protecting competitors is antithetical to the aims of antitrust.

Corwin Edwards writes\(^{108}\):

People will not compete without some hope of success; and successful competition necessarily diverts business from rivals. To make such diversion unlawful is tantamount to a complete prohibition of the tactics of making price reductions or price increases that result in nonuniform prices. It is to forbid limited experiment with new price policies, adjustment of prices to varying conditions of demand, and response to competitive pressures that are neither general nor strong enough to induce a general price change. It is to reduce competition, not to protect it.

Similarly the Attorney General's Committee recommends\(^{109}\):

...that analysis of the statutory "injury" center on the vigor of competition in the market rather than hardship to individual businessmen. For the essence of competition is a contest of trade among business rivals in which some must gain while others lose, to the ultimate benefit of the consuming public. Incidental hardships to individual businessmen in the normal course of commercial events can be checked by a price discrimination statute only at the serious risk of stifling the competitive process itself.

\(^{107}\) Dept. of Justice Report, p. 213.


\(^{109}\) Attorney General's Report, p. 164 (footnote omitted).
The Committee argues that:\(^{110}\):

...it is not "injury" to competitors but adverse effects on "competition with" parties privy to discriminations that the statute expressly forbids. Hence we believe that criteria of competitive effect which focus exclusively on individual competitors' sales or profits rather than the health of the competitive process literally go beyond the terms of the law.

More recent decisions have focussed on competition, bringing the Act in line with other anti-trust statutes. The Supreme Court in *Automatic Canteen Co. v. F.T.C.*\(^{111}\) declared that Robinson-Patman enforcement could "help give rise to a price uniformity and rigidity in open conflict with the purposes of other antitrust legislation". The Court recognised a "duty to reconcile" the Robinson-Patman Act "with the broader antitrust policies that have been laid down by Congress"\(^{112}\). The Seventh Circuit in *Anheuser Busch, Inc. v. F.T.C.* states\(^{113}\):

The Act is really referring to the effect upon competition and not merely upon competitors....In this respect S. 2(a) must be read in conformity with the public policy of preserving competition, but it is not concerned with mere shifts of business between competitors. It is concerned with the substantial impairment of the vigor or health of the contest of business, regardless of which competitor wins or loses. The competition which is sought to be protected by this section is a contest between sellers for the buyer's business, because, "competition is, in its very essence, a contest for trade".

The Act may therefore protect a competitor only when the survival of that competitor is necessary to ensure competition in the market.

(4) **The Standard of Injury to Competition**

The term "substantially" in the text means no more then that the competitive injury be more than minimal. While the Supreme Court

\(^{110}\) *ibid*, at p. 165 (footnote omitted).

\(^{111}\) *Automatic Canteen Co. v. F.T.C.*, 346 U.S. 61,63 (1953).

\(^{112}\) 346 U.S. at 74.

\(^{113}\) *Anheuser Busch, Inc. v. F.T.C.*, 289 F2d 835,840 (7th Cir. 1961).
employed a low threshold test in \textit{F.T.C. v. Morton Salt Co.}, subsequent rulings have required a greater showing of competitive injury. The \textit{de minimus} principle is employed to exclude from the jurisdiction of the Act those discriminations that have insignificant competitive impact. In \textit{E Edelmann & Co. v. F.T.C.} the Court said\textsuperscript{114}: "it is implicit in the Act that discriminations which are negligible and which at best have a remote effect on competition are not within the prohibitions". The Seventh Circuit construed the Act to require "substantial, not trivial or sporadic, interference with competition to establish a violation of its mandate"\textsuperscript{115}. A higher threshold of competitive injury is consistent with the standards of the Sherman Act.

\textbf{(5) Present and Future Effects to be Considered}

Both present effects and likely future events may be examined to determine competitive injury. This is justified by the term 'may be' substantially to lessen competition. Controversy, fuelled by the \textit{Corn Products Refining Co. v. F.T.C.} and \textit{F.T.C. v. Morton Salt Co.} decisions\textsuperscript{116}, occurred over the extent that future harm may be inferred from present events. In \textit{Corn Products} the Court said\textsuperscript{117}:

\begin{quote}
...S. 2(a) does not require a finding that the discriminations in price have in fact had an adverse effect on competition. The statute is designed to reach such discriminations "in their incipiency", before the harm to competition is effected. It is enough that they "may" have the prescribed effect... The use of the word "may" was not to prohibit discriminations having "the
\end{quote}

\textsuperscript{115} \textit{Minneapolis-Honeywell Regulator Co. v. F.T.C.}, 191 F.2d 786,790 (7th Cir. 1951).
\textsuperscript{117} \textit{Corn Products Refining Co. v. F.T.C.} 324 U.S. 726,738 (1945), (emphasis supplied).
mere possibility" of these consequences, but to reach those which would probably have the defined effect on competition.

The Court then added:

...The statute does not require that the discriminations must in fact have harmed competition, but only that there is a reasonable possibility that they "may" have such an effect.

This raised the question of whether the plaintiff must show there is a "reasonable probability" or a "reasonable possibility" of future harm. The controversy, however, has become academic as Courts have used the terms interchangeably. The Seventh Circuit in Minneapolis-Honeywell Regulator Co. v. F.T.C. 118 distinguished between the insufficient "mere possibility" and the adequate "reasonable probability or even possibility".

(6) Onus of Proof

The onus of proving competitive injury rests with the parties seeking to establish a violation of Section 2(a). The Second Circuit placed this burden on the discriminator in its Samuel H. Moss, Inc. v. F.T.C. decision 119 by a literal reading of S. 2(b) which places the burden of rebutting a prima-facie case of discrimination upon the person charged with a violation. This 'presumption' doctrine, (that the discrimination is presumed to cause competitive injury until shown otherwise by the discriminator) was overruled by the Supreme Court in its Automatic Canteen Co. v. F.T.C. decision 120. The Supreme Court construed S. 2(b) as merely a cautionary proviso "making it clear that ordinary rules of evidence were to apply in Robinson-Patman Act

118 Minneapolis-Honeywell Regulator Co. v. F.T.C., 191 F.2d 786,792 (7th Cir. 1951).
119 Samuel H. Moss, Inc. v. F.T.C., 148 F.2d 378,379 (2nd Cir. 1945).
proceedings".

(7) **Causation in Primary and Secondary Line Injury**

In *Shore Gas & Oil Co. v. Humble Oil & Refining Co.*,\(^{121}\) the Court held that the competitive injury must proximately result from the defendant's price discrimination - the injury must be the **effect** of the discrimination.

The causal connection between the discrimination and the injury to competition varies depending upon whether the injury is to primary line or secondary line competition. A discrimination combines two elements - a lower price to some buyers which causes injury to competitors of the seller, and a disparity in prices charged by the seller to different buyers giving the buyer who receives the lower price a competitive advantage over the buyer who does not. In *Shore Gas & Oil* the Court said\(^{122}\):

...to establish the necessary causative link between the price difference and the injury to competitors and competition, it must be shown that high prices aided the injurious low prices and enabled defendant to charge them. Conversely, if no relationship is shown between prices in the low price area and prices in other areas, the injured party's case fails for lack of causation.

and further\(^{123}\):

When a seller underbids a competitor, thereby injuring him, the injury is an 'effect' of discrimination only if the low price is supported by other prices and their profits, wherever charged. Otherwise, the low price alone has caused the injury and the price discrimination is but incidental. Thus if it is shown that the low bid is below cost, it is fairly inerrable that profits made on other prices financed the complained-of low price. If the price is completely self-sufficient, it may be inferred that no


\(^{122}\) 224 F. Supp. at 925-926.

\(^{123}\) *id.*
relationship between the high and low prices exists, and therefore that the discrimination has not the proscribed 'effect'.

And in secondary line cases\(^{124}\):

In the common "secondary" or buyer's line injury case, the causal relationship between discrimination and injury to competition is obvious: defendant's difference in price to buyers places the one discriminated against at a competitive disadvantage, consequently prejudicing fair, vigorous competition in the affected market.

Finally, before we approach the difficult question of how competitive injury is to be determined, this cautionary statement from the Supreme Court should be noted\(^{125}\):

In appraising the effects of any price cut or the corresponding response to it, both the Federal Trade Commission and the Courts must make realistic appraisals of the relevant competitive facts. Invocation of mechanical word formulas cannot be made to substitute for adequate probative analysis.

3.13 DETERMINING PRIMARY LINE INJURY

The requisites to establish primary-line injury are presently confused. The Act requires that the price discrimination have the effect of injuring competition. This seems to require two causal elements. First, a low price which injures competition, and second, a finding that the higher price in one market supported the lower price in the other market, (so that the discrimination, and not merely the low price, had the injurious effects)\(^{126}\).

\(^{124}\) id.

\(^{125}\) F.T.C. v. Sun Oil Co., 371 U.S. 505, 527 (1963), (emphasis supplied).

\(^{126}\) A competitive relationship need not exist between buyers in primary line cases. The Supreme Court overruled the Seventh Circuit in to affirm this point. The Act therefore applies to cases of territorial price discrimination even though buyers in the two markets do not compete for sales. F.T.C. v. Anheuser Busch, Inc., 363 U.S. 536, 546 (1960).
Analysis of primary-line injury can be divided into three parts; the requirement of inter-area subsidization, the element of predatory intent, and indicia used to determine actual injury to competition.

(1) **Causation in Primary Line Cases: Market Subsidization**

Historically, Courts have focussed on the first causal relationship that a low price must cause injury to competition, and consequently case history is confused on the necessity to establish a causal link between the higher and lower price. Different standards apply depending on whether the case is a private suit, and on whether there has been a finding of intent to destroy a competitor.

(a) **Determining Inter-area Subsidization.** Often subsidization can be assumed from the presence of below-cost sales or sustained underselling. According to Rowe\(^{127}\), while subsidization may be presumed from the existence of differential prices, this is a presumption which may be rebutted. In *Lloyd A. Fry Roofing Co. v. F.T.C.* the Seventh Circuit said "Congress and the cases assume that the higher price to purchasers supports the lower price to others"\(^{128}\), yet the same Court in *Dean Milk Co. v. F.T.C.* criticised the F.T.C. for failing to produce evidence of subsidization\(^{129}\).

The Ninth Circuit in *William Inglis & Sons Baking Co. v. I.T.T. Continental Baking Co.*\(^{130}\) took the view that a discrimination was necessary under the Robinson-Patman Act, but there need be no causal relation between the discrimination and the injury to competition. While this view makes more sense and equates the approaches of the Robinson-

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\(^{127}\) Rowe, *op. cit.*, pp. 166-168.

\(^{128}\) *Lloyd A. Fry Roofing Co. v. F.T.C.*, 1 F.2d 277 (7th Cir. 1966).

\(^{129}\) *Deans Milk Co. v. F.T.C.*, 395 F.2d 696 (7th Cir. 1968).

\(^{130}\) *William Inglis & Sons Baking Co. v. ITT Continental Baking Co.*, 668 F.2d 1014 (9th Cir. 1981).
Patman and Sherman Acts to predatory pricing, it does make the price discrimination requirements of the Robinson-Patman Act almost superfluous.

Further Kintner notes that the Courts have generally dispensed with both aspects of causation, (i.e. that the low prices have caused the injury and that these low prices were subsidized by higher prices elsewhere) when presented with evidence of predatory intent.\(^{131}\)

(b) **Private Enforcement.** In cases for private damages a finding of subsidization may be necessary.\(^{132}\) The 'anti-trust injury' doctrine developed by the Supreme Court in *Brunswick Corp. v. Pueblo Bowl-O-Mat, Inc.*,\(^{133}\) demands that the plaintiff in primary line cases must show that he has been injured "by reason of" the differential pricing, not simply that the differential pricing is illegal and that the plaintiff has been injured. It seems likely therefore that a dichotomy exists in the approaches of private and public suits.

(c) **Rebuttal of an Assumption of Inter-area Subsidization.** Where the discrimination results from different conditions operating in each market, an assumption of inter-area subsidization may be unwarranted. In *Balian Ice Cream Co. v. Arden Farms Co.*,\(^{134}\) the Ninth Circuit exonerated a territorial discrimination because of a lack of 'causal connection' or 'relation' between the supplier's prices in the different geographic locations. The Court found "the prices in each area are based upon the


\(^{134}\) *Balian Ice Cream Co. v. Arden Farms Co.*, 231 F.2d 356,367 (9th Cir. 1955), *cert. denied* 350 U.S. 991 (1956).
cost of production and competitive conditions based upon like products manufactured by others".

(d) **Inter-area Subsidization Not a Sufficient Condition.** Finally two cases indicate that a finding of subsidization alone is insufficient to establish a violation of the Act. In *Borden Co. v. F.T.C.* the temporary nature of the discriminatory below-cost pricing was found inadequate to support a case against the defendant. In *National Dairy Products Corp.* one count involved the introduction of a new brand of ice-cream topping using various promotional tactics. Despite the presence of below-cost sales requiring subsidization, the Hearing Examiner dismissed the complaint because of the pro-competitive impact of the new product.

(2) **Predatory Intent**

(a) **The Utah Pie Case and Predatory Intent.** Predatory intent means "intent to destroy one's competition with resort, if necessary, to means not justified by ones own short-term self interest." The Supreme Court in *Utah Pie v. Continental Baking Co.*, made it clear that predatory intent coupled with a price discrimination establishes a violation:

> It seems clear to us that the jury heard adequate evidence from which it could have concluded that Pet had engaged in predatory tactics in waging competitive

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135 *Borden Co. v. F.T.C.*, 339 F.2d 953 (7th Cir. 1964).


warfare in the Salt Lake City Market. Coupled with the incidence of price discrimination attributable to Pet, the evidence as a whole established rather than negated the reasonable possibility that Pet's behavior produced a lessening of competition proscribed by the Act.

Despite the weight that this case should carry, many lower Courts have not been willing to accept the Supreme Court's decision. This has placed the question of predatory intent in a state of flux.

The reluctance to accept this precedent stems from the peculiar facts of the case. The victim, Utah Pie, had an almost monopolistic hold on the market because of its substantial location advantages. Utah Pie itself initiated many of the price cuts and at almost all times maintained a price lower than its competitors, whose own price cuts were more defensive than aggressive. Indeed, Utah Pie remained a healthy company during the period of predation, with increased profits, increased sales, and a market share that rarely fell below 40%, whereas of the three competitors, only Pet had a market share over 20%, the other two having shares around 10%.

(b) Establishing Predatory Intent. Predatory intent may be determined directly through explicit statements of intent to ruin ones competitors\textsuperscript{139}, or it may be inferred by a seller's resort to anti-competitive practices\textsuperscript{140}. This inference can be supported by reference to -

(i) the size of the seller,

(ii) an independent source of finance to fund the predation,

(iii) sales below cost,

(iv) deep and sustained underselling (even when these sales are not below cost),

\textsuperscript{139} Eg., see Porto Rican American Tobacco Co. v. American Tobacco Co., 30 F.2d 234 (2d Cir.), cert. denied 279 U.S. 858 (1929).

\textsuperscript{140} eg. Utah Pie Co. v. Continental Baking Co., 386 U.S. 685,697 (1967). The defendant, Pet, was condemned partially for the use of an industrial spy.
(v) the number and vigor of competitors\textsuperscript{141}.

Below-cost pricing may indicate predatory intent, which further indicates injury to competition. (This is called the "double inference" rule). In \textit{Utah Pie Co. v. Continental Baking Co.}, the Supreme Court found some of Continental's sales were less then its "direct cost plus an allocation for overhead" and that this evidenced predatory intent\textsuperscript{142}. The average total cost test, however, has been supplanted by a marginal cost test developed by Professors Areeda and Turner\textsuperscript{143}. This test has found favour in recent decisions although it still has not been fully accepted\textsuperscript{144}.

In \textit{William Inglis \\& Sons Baking Co. v. ITT Continental Baking Co.}, the Ninth Circuit employed the Areeda and Turner test, although modified to include factors other than price\textsuperscript{145}:

A plaintiff may establish the required effects on competition in a primary line case even though the defendant's prices were shown to be above marginal cost. However, unless the plaintiff proves that the prices were below the defendant's average variable cost, the plaintiff bears the burden of establishing that the anticipated benefits of the prices depended on their anticipated destructive effect on competition. If the

\begin{footnotes}
\item 386 U.S. at 696 n. 12.
\item P. Areeda and D. Turner, \textit{Predatory Pricing and Related Practices} under S. 2 of the Sherman Act, 88 \textit{Harvard Law Review} 697, (1975). This test was developed for use in predation cases brought under Section 2 of the Sherman Act although it is equally applicable to cases involving primary line injury under the Robinson-Patman Act. See discussion of this test, \textit{infra}, pp. 238-241, and references cited at p. 241 fn. 33.
\item eg. See Californian Computer Products, Inc. v. IBM Corp., 613 F.2d 727 (9th Cir. 1979); Janich Bros. v. American Distilling Co., 570 F.2d 848 (9th Cir. 1977), cert. denied, 439 U.S. 829 (1978); Pacific Eng'r \\& Prod. Co. v. Kerr-McGee Corp., 551 F.2d 790 (10th Cir.), cert. denied, 434 U.S. 879 (1977); Hanson v. Shell Oil Co., 541 F.2d 1352 (9th Cir. 1976); International Air Indus., Inc v. American Excelsior Co., 517 F.2d 714 (5th Cir. 1975), cert. denied, 424 U.S. 943 (1976).
\item \textit{William Inglis \\& Sons Baking Co. v. ITT Continental Baking Co.}, 668 F.2d at 1041.
\end{footnotes}
plaintiff does prove pricing below average variable cost, 
the burden shifts to the defendant to establish a 
legitimate business justification for its conduct.

The presumptions of per se legality or per se illegality drawn from the 
Areeda and Turner test are therefore rebuttable.

The Fifth Circuit also employed a modified average variable cost 
test in *International Air Indus, Inc. v. American Excelsior Co.*, 146:

...as a matter of law, a plaintiff must at least show 
that either 1) a competitor is charging a price below his 
average variable cost in the competitive market or 2) the 
competitor is charging a cost below its short-run profit-
maximising price and barriers to entry are great enough 
to enable the discriminator to reap the benefits of 
predation before new entry is possible.

(c) *Is 'Intent' a Sufficient Condition?* Like 'intent to 
monopolize', predatory intent is very difficult to distinguish from pro-
competitive behaviour. Where it is established however, it may provide a 
strong indication of likely future events. Indeed, in *Utah Pie Co. v. 
Continental Baking Co.*, the Supreme Court said that cases where 
predatory intent was established were easy 147. It may also be used to 
refute a 'good faith' meeting competition defence.

Although inconsistent with the Supreme Court's *Utah Pie* decision, 
many Courts have found that predatory intent alone, without any finding 
of present or likely future adverse effect on competition, would be 
isufficient to establish a violation of S. 2(a). The Third Circuit in 
*O. Hommel Co. v. Ferro Corp.* 148, did not consider what constituted

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147 Referring to cases involving blatant predatory price discriminations employed with the hope of immediate destruction of a 
competitor, the Supreme Court said "on the question of injury to 
competition such cases present courts with no difficulty, for such 
pricing is clearly within the heart of the proscription of the Act". 386 U.S. at 702.

predatory pricing because there was affirmative evidence of no adverse effect from the discrimination and therefore no basis for the jury to infer such adverse effect.

(d) Is 'Intent' a Necessary Condition? While it seems that predatory intent alone is not sufficient to establish a violation of S. 2(a), recent Court decisions indicate that predatory intent is a necessary element in any prosecution. Courts have generally ignored Utah Pie where the Supreme Court declared that factors other than predatory intent could support a finding of competitive injury\textsuperscript{149}, and instead followed the Seventh Circuit's decision in Anheuser Busch that a finding of predatory intent was necessary to establish a S. 2(a) violation\textsuperscript{150}. The Ninth Circuit in William Inglis & Sons Baking Co. v. ITT Continental Baking Co.\textsuperscript{151} apparently differentiated between the requirements of the Sherman Act and the Robinson-Patman Act saying that an offence under the Robinson-Patman Act might "perhaps be established without proof of predatory intent or predatory pricing". In the case, however, the Court insisted on a finding on both intent and conduct tests similar to the Sherman Act\textsuperscript{152}.

\textsuperscript{149} The Supreme Court said "In this case there was some evidence of predatory intent with respect to each of these respondents. There was also other evidence upon which the jury could rationally find the requisite injury to competition". 386 U.S. at 702-703.

\textsuperscript{150} Anheuser Busch, Inc. v. F.T.C., 289 F.2d 835 (7th Cir. 1961).

\textsuperscript{151} 668 F.2d at 1042.

\textsuperscript{152} See also the Ninth Circuit's decision in Janich Bros. v. American Distilling Co., 570 F.2d 848 (9th Cir. 1977), cert. denied 439 U.S. 829 (1978), where the Court observed that the tests for competitive injury were identical to the predation tests used in Sherman Act cases. See also International Air Indus., Inc v. American Excelsior Co., 517 F.2d 714 (5th Cir. 1975), cert. denied 424 U.S. 943 (1976). If this is true, then Hovenkamp is correct in his assertion that the Robinson-Patman Act demands a more stringent test then the Sherman Act because of its jurisdictional limitations. Hovenkamp, op.cit., p. 324.
(3) Determining Competitive Injury in the Absence of Predatory Intent

In early decisions the F.T.C. and reviewing Courts have been willing to find competitive injury even where predatory intent is not found. These cases are instructive as they focus on the injury to competition tests which are often obscured in cases involving predatory intent.

(a) Diversion of Trade. Perhaps the most significant case on determining competitive injury in the absence of predatory intent is the F.T.C.'s Dean Milk Co. case. Chairman Dixon suggests that actual effects caused by the price discrimination coupled with reasonably foreseeable anti-competitive results constitute a violation of S. 2(a). The actual effects might be a significant diversion of trade away from competitors to the discriminator or diminishing profits to competitors of the discriminator (caused by loss of sales from the diversion of trade, the necessity to lower prices to prevent the diversion of trade, or the higher average costs that result from operating at a lower level of production). Competitive injury is found where these effects are coupled with a trend towards further losses of business or profits, and increased concentration of business in the market.

In Dean Milk Co. the F.T.C. employed diversion of trade as the beginning point of market analysis. The test has developed substantially from when it was first used by the F.T.C. and confirmed by the Second

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154 Dean Milk Co., 68 F.T.C. 710 (1965). This represents another case reversed on appeal because of a lack of predatory intent. Dean Milk Co. v. F.T.C., 395 F.2d 696 (7th Cir. 1968); See also Borden Co. v. F.T.C., 381 F.2d 175 (5th Cir. 1967); Anheuser Busch, Inc. v. F.T.C., 289 F.2d (7th Cir. 1961); Minneapolis-Honeywell Regulator Co. v. F.T.C., 191 F.2d 786 (7th Cir. 1951), cert. dismissed 344 U.S. 206 (1952).
Circuit in the Samuel H. Moss, Inc. v. F.T.C. decision. It is not the final proof of competitive injury as was considered in the Minneapolis-Honeywell Regulator Co., decision. Diversion of trade meant both the increase in sales resulting from the price reduction and the retention of trade that would have been lost but for the price reduction (i.e., it covered defensive price reductions). The F.T.C. considered that a diversion of trade to the discriminator resulting from a discrimination impeded the growth of competitors and enabled the discriminator to protect his competitive situation, and therefore caused injury to competition. The Seventh Circuit reversed, holding that diversion of trade alone is insufficient to permit a finding of competitive injury in the absence of evidence of an actual lessening in the vigour of competition. Clearly both pro-competitive and anti-competitive price discrimination may cause a diversion of trade to the discriminator and therefore this test alone cannot be used to identify anti-competitive price discrimination.

Anheuser Busch, Inc. marks the next development in the diversion of trade test. The F.T.C. defined diversion of trade as a substantial shift in market shares. The F.T.C. Order was finally set aside by the Seventh Circuit as the diversion was of a temporary nature and unlikely to cause competitive injury. The Seventh Circuit found that although the respondent's price cuts increased their market share from 12.5% to 36.6%, the respondent's share dropped to 17.5% eleven months


156 Minneapolis-Honeywell Regulator Co., 44 F.T.C. 351, 397 (1948), 191 F.2d 786 (7th Cir. 1951).

157 See also Edwards, supra, p. 78.

158 Anheuser Busch, Inc., 54 F.T.C., 277 (1957) at 299-300.

159 Anheuser Busch, Inc. v. F.T.C., 289 F.2d 835, 840, 843 (7th Cir. 1961).
after the retraction of the second price reduction, and a competitor's market share had grown from 29.4% before the first price reduction to 43.2% eleven months after the retraction of the second price reduction. The Seventh Circuit reaffirmed that a diversion of trade must be permanent in its review of Borden Co. and again set aside an F.T.C. Order\textsuperscript{160}. Of interest in the Borden case was that although the sales of a competitor's house brand milk were eliminated, the profits of that company (Quality Dairy) increased as it also handled Borden's milk and received a commission for the delivery of Borden's milk to A & P. The F.T.C. concentrated on the adverse effect that the withdrawal of Quality Dairy's product would have on the market rather than the adverse effect on Quality Dairy itself\textsuperscript{161}.

(b) **Loss of Profits.** Chairman Dixon considered the 'loss of profits' test as an alternative to the diversion of trade test. Where a firm lowers its prices in a market, trade may be diverted to it, or rivals may respond with competitive price reductions. Lower profits may result either from lower prices or, where sales are diverted, from a lower sales level and from operating at an inefficiently low level of production. As with the diversion of trade test, loss of profits alone may not indicate competitive injury and should be treated as the starting point of any market analysis. Where previous profit levels were high, loss of profits may indicate a move to a more competitive situation. This test implies that selling below the costs of a competitor may therefore be anti-competitive even though the price exceeds the costs of the discriminator and is not classed as predatory by the Areeda and Turner test.

(c) **A Deteriorating Price Structure.** One test derived from Utah

\textsuperscript{160} Borden Co. v. F.T.C., 339 F.2d 953,957 (7th Cir. 1964).

Pie Co. v. Continental Baking Co., 162 is the presence of a declining price structure. Where promotions and price cuts lead to significantly lower prices, the Courts may infer that a small company will, in the future, 'feel the financial pinch' of these price cuts and become a 'less effective competitor'.

(4) General Conditions For Primary Line Injury

A review of cases involving territorial price discrimination shows the following common characteristics163:

(i) There was a small local competitor (usually a single competitor) in the price reduction area competing with a much larger, well entrenched or overpowering competitor doing business in numerous areas.

(ii) The small competitor's sales were confined to the price reduction area.

(iii) Generally, the price reduction undercut that of the small competitor, and in many cases the discriminator's price was well below its cost and in effect was subsidized by its operations elsewhere, the reduction in the one area being to a point so low that the small, usually sole, competitor there could not effectively compete.

(iv) The price reduction resulted in the small competitor losing not only sales but channels of distribution and outlets through which it could make sales.

(v) The elimination or crippling of a highly vulnerable, small competitor either would have led, or did lead, to a monopoly by the discriminating seller in the price reduction area, since there was only a single competitor in the area of the price reduction.

162 386 U.S. 699-700.

(vi) The discrimination was continued a sufficiently long time either to cause elimination of the competitor from a particular product line or impair seriously its ability to compete.

(vii) There was a clear design to eliminate or destroy a competitor, as plainly established by documents, by undercutting price reduction, by the sales below cost or other circumstances surrounding the reduction, and a likelihood of success.

(5) Rebutting an Inference of Primary Line Injury.

A prima-facie proof of competitive injury may be rebutted by showing that competition has not been impaired in the market, or that the reduction of competition was due to factors other than the price reduction. Rowe identifies some of these considerations\(^{164}\):

(i) Decline in the seller's own percentage share of the market, notwithstanding his price differentials.

(ii) Minor over-all market position of the seller.

(iii) Growth of the seller's competitors, in terms of their market shares, their absolute sales volume, or simply by their sales to full capacity.

(iv) Prevalence of comparable price variations on the part of competitors.

(v) Inroads by sellers on each other's customers and/or customer switches among sellers.

(vi) Ease of entry by competing sellers into the pertinent market.

(vii) Keenness of competition among the sellers, or overall dynamism in the market.

(viii) Competition by seller against strongly entrenched regional competitors.

\(^{164}\) Rowe, op. cit., p. 161.
(ix) Aim by seller to improve his deteriorating market position, or temporary price experimentation to this end.

Many of these factors were present in Utah Pie \(^{165}\) causing the Fifth Circuit to distinguish that case in its Borden Co. v. F.T.C. decision \(^{166}\), saying that the expansion of sales and continued profitability of the competitor did not preclude a finding of competitive injury where predatory intent was found. (This seems a misinterpretation of the Utah Pie decision which found the requisite competitive injury even without regard to predatory intent) \(^{167}\).

A seller may also defend himself by showing that there is no causal relationship between the discrimination and the adversities of the rivals. Even if competition were impaired, the seller may show\(^ {168}\):

(i) that this effect resulted from the seller's successful marketing techniques other than the low price,

(ii) that the adversities were due to the internal troubles or competitive inertia of rivals, and not by the low price. In Anheuser Busch the Court of Appeals identified internal troubles of two competitors\(^ {169}\). One sold a beer which was "badly named, poorly merchandised, bitter in taste and 'wild'", the other's management maintained a "highly liquid cash position at the expense of renewal or replacement of productive facilities". The rationale of both defences

\(^{165}\) The Supreme Court rejected the Court of Appeal's reliance on the health of Utah Pie to disprove competitive injury, saying "But we disagree with its apparent view that there is no reasonable possible injury to competition so long as the volume of sales in a particular market is expanding and at least some of the competitors in the market continue to operate at a profit". 386 U.S. at 702.

\(^{166}\) Borden Co. v. F.T.C., 381 F.2d 179, n. 12.


\(^{168}\) Rowe, op. cit., p. 163-168.

\(^{169}\) 289 F.2d 837, n. 4,5.
is that the Courts will not condemn a lower price if it results from the more efficient practices of the seller or the less efficient practices of the rivals.

(iii) that there exists no causal connection between the discrimination and the injury in geographic price differentiation. (See the earlier discussion on this point).

(6) **Competitive Injury and Differentiated Products**

The Supreme Court in **F.T.C. v. Borden & Co.** indicated that differentials between branded and non-branded goods were to be considered under the injury to competition and cost-justification provisions of the Act, and not under the 'like grade and quality' provision. The **Anheuser Busch, Inc.** case focuses on the issue of premium goods in a primary-line context. Anheuser Busch lowered the price of its premium 'Budweiser' beer to exactly match the prices of local non-premium beers causing a substantial diversion of trade away from competitors. In its initial decision the F.T.C. emphasized that 'Budweiser' is a "premium" beer and that the company's price reduction to the level of prices charged for the local beers actually undercut those prices.

(7) **Industry-wide Pricing Systems.**

While largely an academic topic because of the F.T.C.'s failure to pursue delivered pricing systems, nevertheless delivered pricing deserves mention because of the impact that these practices may have on

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171 **Anheuser Busch, Inc.**, 54 F.T.C. 277, 302 (1957). The case was finally decided in favour of Anheuser Busch, because of the absence of predatory intent, the temporary nature of the diversion of trade and the presence of other factors adversely influencing the competitive position of competitors.
competition if practiced on an industry-wide basis, (either because of conscious-parallelism or overt collusion). The F.T.C., in ruling against the collusively-adopted multiple-basing point system operating in the cement industry, said:\(^\text{172}\):

...each reciprocally waives the advantages and neutralizes the disadvantages which it has in certain consuming areas....in order that there may not anywhere be genuine competition in price between producers which, except for such reciprocal waiver and neutralization, would be in normal and active competition in price.

The Commission's 1948 Statement of Policy Towards Geographic pricing policies redefined injury to competition arising from industry-wide pricing practices:\(^\text{173}\):

Injury to competition through common use of a discriminatory pricing pattern by sellers appears...when discrimination is an inherent part of the collusive arrangement through which competition is set aside. Thus the test of injury on the selling side of the market is to be found in collusion or in tendencies toward monopoly.

The Commission sought to attack both "conscious parallelism" and overt collusion:\(^\text{174}\):

...the obvious fact that the economic effect of identical prices achieved through conscious parallel action is the same as that of similar prices achieved through overt collusion.

Rowe and the Attorney General's Committee have disagreed with the attack on parallel behaviour using the Robinson-Patman Act. Rowe states:\(^\text{175}\):

Thereby price quotations by any one of several sellers employing the same differential pricing practice, whether by means of freight absorption, quantity discounts or otherwise, could become individually vulnerable under the Robinson-patman Act as creating "injury to competition" through this nonconspiratorial yet "common use of a

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\(^{172}\) Cement Institute, 37 F.T.C. 87, 124 (1948).


\(^{174}\) \textit{ibid}, at p 5348.

\(^{175}\) Rowe, \textit{op. cit.}, p. 170.
discriminatory pricing pattern"... But since the vice of the formula prices questioned by the Federal Trade Commission lies in collusion rather than price differentiation, this rationale becomes questionable for lack of a causal nexus between the challenged individual discrimination in price and the asserted competitive impairment.

And the Attorney General's Report notes 176:

Since this sort of "injury" is the inevitable consequence of every price-fixing scheme, any element of price discrimination in "delivered" price quotations remains a largely incidental consequence of the real antitrust offense.

The Supreme Court has been willing to uphold orders against collusively-adopted pricing schemes under the Robinson-Patman, Sherman, and Federal Trade Commission Acts 177, but has remained unconvinced that conscious parallelism equates with overt collusion 178. To do so would be to rule against suspected conspiracy without actually having to prove the conspiracy.

(8) **Promotional pricing**

A final area of analysis that is relevant in primary line cases is promotional pricing. A new seller may use promotional pricing to establish a new product. The addition of this product may increase competition in the market. However, promotional pricing may disguise anti-competitive predatory pricing. In National Dairy Products Corp., Commissioner Jones sought to identify some tests to distinguish anti-


178 Although the Supreme Court affirmed a Court of Appeal's Order condemning individual quotations of "delivered" prices as "unfair methods of competition", when adopted independently by a single seller with the knowledge that his rivals acted likewise. Triangle Conduit & Cable Co. v. F.T.C., 108 F.2d 175 (7th Cir. 1948), affirmed without opinion, Clayton Mark & Co. v. F.T.C., 336 U.S. 956 (1949). The Attorney General's Report, however, rejects the contention that this case implies that delivered pricing systems adopted without collusion constitute a violation of Section 5 of the Federal Trade Commission Act, p. 216.
competitive promotions\textsuperscript{179};

(i) Most important, where the product is sold 'below-cost' and especially where competitors have difficulty meeting this price.

(ii) Where the seller would need a 'relatively long period' to recoup the cost of the promotion out of future sales to the market.

(iii) Where the promotion is unlimited in quantity and runs for a long period.

(iv) Where the seller has previously unsuccessfully tried to improve his market share, indicating the public has rejected his product.

(v) Where other sellers do not have the capacity to meet the promotional activity.

(vi) Where the seller has other means of promoting the product.

3.14 SECONDARY AND TERTIARY LINE INJURY

The primary objective of the Robinson-Patman Act was to curb the abuse of buying power by large chain stores. The effectiveness of the Act to achieve this objective hinges on the competitive injury test. Analysis of this test, as it relates to secondary line injury, can be separated into three parts; 1) establishing a competitive relationship between the recipient of the discrimination and disfavoured buyers, 2) establishing inimical competitive effects caused by the discrimination, 3) injury to tertiary line injury and beyond.

1) \textbf{Establishing a Competitive Relationship Between Buyers}

Injury to secondary line competition results when discounts are granted to one buyer but are denied to another, giving one buyer a competitive advantage over the other. It follows that there must be some

\textsuperscript{179} National Diary Products Corp., 70 F.T.C. 79 (1966).
competitive contact between buyers if secondary line injury is to occur. However, competitive contact may not exist because the buyers are segregated geographically, because the buyers operate in separate product markets, or because they operate at different functional levels.\textsuperscript{180}

(a) \textbf{Geographic Distinctions}. Where buyers are separated by location and do not compete for the same customers, there can be no competitive injury caused by a discrimination in price between them.\textsuperscript{181} The issue is to identify a territory such that no buyer inside the territory is in competition with buyers outside the territory, or at least to minimise the impact of such differentials on competition between these buyers. This problem is particularly relevant to zone-delivered pricing systems where buyers situated on the border between two zones are in competitive contact.

Some contact between buyers in different zones is inevitable, as recognised by the F.T.C. in Pure Oil Co.\textsuperscript{182}: "no matter what area may be chosen, there will always be fringe or peripheral effects on the border line of such areas between customers within the area and customers without" for "to hold otherwise would require uniform prices everywhere".

How then is a trade zone defined such that price differentials between zones will not cause competitive injury? One approach is to use natural boundaries on the assumption that these boundaries also represent distinct competitive areas. Chairman Dixon's majority opinion

\textsuperscript{180} See generally, Rowe, \textit{op. cit.}, pp. 173-180.

\textsuperscript{181} See National Lead Co. v. F.T.C. 227 F.2d 825,836 (7th Cir. 1955), rev'd on other grounds 352 U.S. 419 (1957).

\textsuperscript{182} Pure Oil Co., F.T.C. Dkt. 6640, p.22 (Jan. 30, 1959).
in Forster Manufacturing Co., reflects this view:\footnote{183}

...if respondents communicated the offer to sell at the 10\% lower price to every buyer located within an arbitrary perimeter surrounding the Pittsburgh marketing area, there would always remain the likelihood that a few buyers located on one side of the "zone" line would compete with buyers located on the other side. To bring all these in, and thus avoid discrimination and competitive injury, respondents would have to continue widening the circle of favored customers, perhaps until they encounter some natural physical barrier (such as a mountain range) to protect the non-favored from the favored buyers.

In another opinion the Court emphasized both natural and economic boundaries but rejected the use of state boundaries as constituting an acceptable trade boundary:\footnote{184} Von Kalinowski summarizes the factors which may indicate whether customers in adjoining or nearby trade areas compete with one another:\footnote{185}

Those factors include: the substantiality of the physical barriers, if any; the actual distance between the various distributors' customers; the degree to which the distributors sell to one another's customers; the keenness of competition; the existence of prior competition between the distributors; the type of business or products involved; and the importance of the price differences.

Thus, while the Courts have not demanded uniform pricing, they have considered the appropriateness of the trade boundaries and sought to minimise any adverse effect that a differential may have on a buyer in a disfavoured zone. One approach to minimising the competitive injury is to create trade zones and then to 'feather out' discounts to those buyers situated outside the zone but in competition with buyers inside the zone. However, by extending the trade zone in this way, a second


'feathering out' might be required, and so on, again resulting in a uniform price everywhere. Commissioner Elman, in his dissenting opinion in American Oil Co., provides the solution:

American could have done what the Commission apparently thinks it was required to do by Section 2(a) - either reduce its prices equally to all of its dealers, or "feather" them out in some way, perhaps diminishing in concentric circles from the starting point of the (price) war, on the theory that the differentials between stations would then not have been sufficiently large to cause any diversion of business between competing stations.

(b) Where Buyers Operate in Different Product Markets. Where buyers operate in different product markets, there is no competitive contact between them. They may do this where the goods are converted to other goods which are resold in another product market. Thus if a button manufacturer classifies his customers according to whether they make dresses or men's suits and discriminates in favour of the former, there can be no competitive injury to secondary-line competition.

Also where one of the buyers is a final consumer of the good, then he no longer in competition with the other buyer in the same product market and a price differential between them may not harm competition.


188 See Secatore's, Inc. v. Esso Standard Oil Co., 171 F.Supp. 665 (D.Mass. 1959) Here Esso sold gasoline at lower prices to a consumer-purchaser then it sold to the plaintiff. The Court found that no secondary-line injury occurred because the favoured buyer was a final consumer of the product. (The Court also found that no primary line injury had occurred even though Secatore's competed with Esso for the resale of gasoline. The Court considered that actual injury was not impaired because the plaintiff had never sold, nor attempted to sell to the consumer-purchaser. The Court did recognise that the lower price effectively prevented the plaintiff from ever entertaining the consumer-purchaser as a customer. Thus potential competition was impaired. However, the Court concluded that if Esso sold to both customers at a (footnote cont. p. 104).
(c) Where Buyers Operate at Different Functional Levels.
Traditionally competition has been viewed as horizontal at different levels of distribution. Manufacturers compete with other manufacturers for the custom of distributors, distributors compete with distributors for the custom of retailers, etc. It follows that as buyers on different functional levels do not compete for the same customers, a seller may set different prices to each distribution level with impunity from the Robinson-Patman Act\textsuperscript{189}.

However, changes in the systems of distribution have clouded this traditional impunity with dual distributors operating at two different levels of distribution, and direct-buying retailers spanning the wholesale and retail functional levels. This complicated topic of functional discounts is therefore considered separately\textsuperscript{190}.

(2) Indicia of Competitive Injury

(a) Inference of Secondary Line Injury. If a discrimination in price exists between two buyers who have a competitive relationship, then the discrimination may cause injury to competition. The major difficulty with examining injury at the buyers level is that the injury may occur from small discounts granted over a long period of time and there exists no easy way of distinguishing discriminations which cause competitive injury. The F.T.C. and Courts have had to rely on broad inferences when applying the Act to secondary line cases. Nevertheless, some tests have been developed to identify anti-competitive price

\footnote{(footnote cont. from p. 103).}

single non-discriminatory per se legal price, the plaintiff could not effectively compete with Esso. Therefore in all cases the plaintiff was excluded from selling to that consumer-purchaser and the discrimination caused no injury to competition).

\textsuperscript{189} Although tertiary line competition may be impaired. See the facts and discussion of \textit{Standard Oil Co. v. F.T.C.}, discussed, \textit{infra}, p. 112.

\textsuperscript{190} \textit{infra}, p. 118.
discrimination. Rowe summarizes these tests$^{191}$:

Essentially, adverse competitive effects are most likely inferred from stable price differentials substantial in amount, as between competing resellers to the same trade, which are in keen competition, and operate on tight profit margins. Conversely, the inference of competitive injury from a supplier's price variations is remotest when the price spread is minimal, concerns a tailored, specialized, or component product, in an industry displaying moderate competition and ample profits.

It is useful to examine the development of these tests and thereby reveal the difficulties of determining secondary line injury. In the early Standard Oil Co. decision$^{192}$, the F.T.C. found the payment of discounts to distributors, who competed with retailers at the retail level, was harmful to competition as the discounts could and had been used to divert large amounts of business from other retailers to the distributors. Standard Oil Co. provides a test in cases where the consumer is sensitive to changes in the price of a particular item.

The F.T.C. v. Morton Salt Co. decision more clearly shows the inherent difficulties of secondary line cases$^{193}$. Morton Salt supplied salt to wholesalers and jobbers who resold to retailers, and also direct to large retailers and chain-stores. Terms of sale include a quantity and volume discount system as listed below for Morton Salt's premium brand - Blue Label:

<table>
<thead>
<tr>
<th>Description</th>
<th>Per Case</th>
</tr>
</thead>
<tbody>
<tr>
<td>Less than car-load purchases</td>
<td>$1.60</td>
</tr>
<tr>
<td>Car-load purchases</td>
<td>$1.50</td>
</tr>
<tr>
<td>5000-case purchases in any consecutive 12 months</td>
<td>$1.40</td>
</tr>
<tr>
<td>50000-case purchases in any consecutive 12 months</td>
<td>$1.35</td>
</tr>
</tbody>
</table>

Only five companies had ever brought sufficient quantities of respondent's salt to obtain the $1.35 per case price, although almost all buyers brought in sufficient quantity to receive the car-load

$^{191}$ Rowe, op. cit., p. 181.

$^{192}$ Standard Oil Co., 41 F.T.C. 263 (1945), aff'd 173 F.2d 210,213 (7th Cir. 1949), order ultimately set aside on other grounds 355 U.S. 396 (1958).

purchase price.

Given that salt is a comparatively small item in a grocer's trade, the Supreme Court was asked to determine whether the discount system could cause injury to competition. The Court found:\(^{194}\)

There are many articles in a grocery store that, considered separately, are comparatively small parts of a merchant's stock. Congress intended to protect a merchant from competitive injury attributable to discriminatory prices on any or all goods sold in interstate commerce, whether the particular goods constituted a major or minor portion of his stock. Since the grocery store consists of many comparatively small articles, there 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 Court then enunciated a rule that where a discount system was large enough to affect the resale price of the good then this was sufficient to support a prima-facie case of injury to competition:\(^{195}\)

In *Corn Products Refining Co. v. F.T.C.*:\(^{196}\) the Court of Appeals condemned a Chicago-plus basing point system in an industry characterized by low profit margins and keen price competition. Buyers of glucose faced the choice of raising their candy prices or absorbing the extra freight costs. The Court noted that "the effect in any case is to reduce the profit margins pro-tanto" in the "absence of any offsetting factor":\(^ {197}\) The F.T.C. retrospectively analysed the competitive injury concept used in the *Corn Products Refining Co. v. F.T.C.* decision:\(^{198}\)

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194 334 U.S. at 49.

195 334 U.S. at 46-47.

196 *Corn Products Refining Co. v. F.T.C.*, 144 F.2d 211 (7th Cir. 1944), aff'd 324 U.S. 726 (1945).

197 324 U.S. at 742.

[A] single seller used a price structure which discriminated among customers by making very substantial price differences upon products which were of great importance to the business of these customers and that, as a consequence of these price differences, injurious effects had appeared in the volume and profits of the concerns paying the higher prices.

This inference has been extended to cases where no resale price competition exists but where profit margins are low. In *E. Edelmann & Co. v. F.T.C.*, the Seventh Circuit said\(^\text{199}\):

It is not necessary that a price advantage be used to lower the resale price and thereby attract business away from the nonfavored competitors. Sales are not the sole indicium that reflects the health of the competitive scene...the purchasers of petitioner's products sold in a market where competition was keen; that these purchasers operated on small profit margins; that many of the purchasers found it expedient to enter into group buying arrangements for the purpose of aggregating their purchases and thereby obtaining higher discounts then they would otherwise receive as ordinary jobbers in contrast to the warehouse distributor.

So strong is this inference of competitive injury, the reviewing Courts refused to accept testimony from disfavoured buyers that they were not injured by the discrimination\(^\text{200}\).

(b) *Rebutting an Inference of Injury: Countervailing Costs*. The Courts have also rejected the argument that the presence of additional costs offsets the advantage of a discriminatory discount and negates a finding of competitive injury. The development of the law in this area is of some interest.

A favoured buyer may incur additional costs because the buyer has

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\(^{199}\) *E Edelmann & Co. v. F.T.C.*, 239 F.2d 152,154,155 (7th Cir. 1956). This emphasis is common to a number of other decisions referred to as the *Automotive Parts* cases. Standard Motor Products, Inc. v. F.T.C., 265 F.2d 674,676 (2d Cir. 1959); Moog Industries, Inc. v. F.T.C., 238 F.2d 43,50 (8th Cir.), 355 U.S. 411 (1956); P&D Mfg. Co. v. F.T.C., 245 F.2d 281 (7th Cir. 1957), cert. denied 355 U.S. 884 (1958); Whitaker Cable Corp. v. F.T.C., 239 F.2d 253 (7th Cir. 1956); P Sorensen Mfg. Co. v. F.T.C., 246 F.2d 687 (D.C. Cir. 1957).

\(^{200}\) See Standard Motor Products, Inc. v. F.T.C., 265 F.2d 674,676 (2d Cir. 1959); Moog Industries, Inc. v. F.T.C., 238 F.2d 43,50 (8th Cir. 1956).
a disadvantage in location, or because he performs additional marketing functions, or simply because he is less efficient than other buyers. At issue is whether a better located or more efficient buyer has the right to the competitive advantage that is denied him if the seller compensates a competitor.

The F.T.C.'s 1948 Policy Statement on Geographic Pricing practices acknowledged that the existence of a disadvantage in location may neutralize an advantage in price and therefore rebut an inference of competitive harm. However, in *Purolator Prod. Inc. v. F.T.C.* the Court took a different view. Purolator claimed that a 4% discount given to affiliated jobbers of warehouse distributors was less then the cost of the internal redistribution of the goods. The Seventh Circuit, however, considered that the countervailing costs were specific to a company's method of operation and "not relevant to disprove competitive injury."

A interesting situation is where the buyer performs additional marketing functions and thereby incurs greater costs then his competitors. In *E. Edelmann & Co.*, the F.T.C. observed that:

> It is true that purchasers receiving larger discounts in instances have rendered bookkeeping service and other promotional services for jobbers and others and even on occasion loaned money to garage operators and service men to set them up as jobbers. These measures inured to the benefit of the affected customers and indirectly to respondent. It is clear, however, that the services performed by recipients of the discounts in the course of sales of their own merchandise to dealers did not justify the discounts.

This decision seems to indicate a dichotomy to the granting of

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203 352 F.2d at 881-882.
discounts in return for the performance of marketing functions. Where the function is merely transferred from the seller to the buyer and the discount approximates the cost of the function, the discount will be presumed legal. (The approach here is identical to that used in the cost justification defence except that it focusses on the buyers costs). However, where the function is intended to better the competitive position of the buyer, he is expected to recoup the cost of the function from his customers and not from the seller.

In Doubleday & Co., a case involving functional discounts, the F.T.C. recognised that "to relate functional discounts solely to the purchaser's method of resale without recognition of his buying function thwarts the competition and efficiency in marketing, and inevitably leads to higher consumer prices." The Opinion allowed the distributive functions of the integrated distributor to be "recognised and reimbursed" by the seller as long as the size of the discount was "reasonably related to the expenses assumed by the buyer." The Commission also expressly disapproved of the Examiner's ruling that "it is only the seller's costs, not the buyer's, which may be shown defensively under the law itself."  

However, the decision in Mueller & Co. shows the substantial shift in the Commission's position on this issue. The Commission found that a price differential recognising a distributor's extra services was not relieved from the conventional criteria of competitive injury when the recipients in fact secured a substantial competitive advantage and the same arrangements were not available to competing distributors. While

206 ibid.
207 52 F.T.C. 209 n.7.
Mueller & Co., deals with functional discounts, the doctrine espoused in that case suggests that a seller may not compensate a buyer for additional functions performed by the buyer, even when the seller is relieved of those functions and thereby receives savings in costs, unless the discount is justified under the cost-justification defence.

Finally, in Knoll Associates, Inc.\textsuperscript{209} the presence of different methods of distribution was found not to justify a discriminatory price between two buyers.

(c) Other Means of Rebutting an Inference of Injury. By way of contrast to the inference rule of F.T.C. v. Morton Salt Co., the F.T.C. dismissed charges in Fred Bronner Corp.,\textsuperscript{210} that a toy supplier's discriminatory prices impaired competition, citing the presence of high mark-ups, the modest size of the differential involved, and the absence of keen competition and high profit margins as preventing an inference of secondary line injury.

A seller may rebut the inference of competitive injury by showing that the injury is not caused by the discrimination. Rowe notes the features which may disrupt the causal nexus\textsuperscript{211}:

(i) intervening economic factors influencing a buyer's resale activities,

(ii) the competitive inertia of the buyer's rivals,

(iii) the availability of the goods at the same or lower price from another source.


\textsuperscript{210} Fred Bronner Corp., 57 F.T.C. 771 (1960).

\textsuperscript{211} Rowe, \textit{op. cit.}, pp. 186-195. In fact Rowe identifies four factors that may disrupt the causal nexus between the discrimination and the injury. However, recent decisions indicate that the presence of countervailing costs does not disturb a finding of competitive injury.
(i) In some cases it has been found that there exists intervening economic factors which influence a buyer's resale activities and these minimise the impact of a discrimination on competition. These intervening factors include price wars\textsuperscript{212}, resale of the seller's commodity as one of several ingredients or components of a new product, or changing market conditions\textsuperscript{213}.

In \textit{Minneapolis-Honeywell Regulator Co. v. F.T.C.}\textsuperscript{214} the Seventh Circuit found no causal relationship between the discriminatory price of a component of a burner (the control) and the price of the burner itself. The Court considered other economic factors dominated a buyer's resale activities, saying\textsuperscript{215}:

\begin{quote}
\ldots where the controls were used in the manufacture of burners, the cost of which was determined by many other factors—cost of the other materials and parts, service, advertising, to mention only a few—it cannot be said that discriminatory price differentials substantially injure competition or there is any reasonable probability or even possibility that they will do so.
\end{quote}

Interestingly, such situations are conceptually similar to the \textit{F.T.C. v. Morton Salt Co.} situation in that they involve the payment of a discount which, in itself, may not have a significant impact on competition but, if combined with other discounts granted to the same favoured buyer, could impair the competitive health of other buyers. However, the Courts have chosen not to apply the same incipiency test that was applied in \textit{Morton Salt}.

(ii) If the injury is caused, not by the discrimination in

\textsuperscript{212} American Oil Co. v. F.T.C. 325 F.2d 101 (7th Cir. 1963), \textit{cert. denied} 377 U.S. 954 (1964).

\textsuperscript{213} See discussion \textit{infra}, p. 151.

\textsuperscript{214} Minneapolis-Honeywell Regulator Co. v. F.T.C. 191 F.2d 786 (7th Cir. 1951), \textit{cert. dismissed} 344 U.S. 206 (1952).

price, but by the competitive inertia of rivals, then there is no causal relationship between the discrimination and the competitive injury. In Alexander v. Texas Co., a gasoline dealer sued his supplier for having granted a discriminatory concession to rival dealers to assist them in coping with a local price war. The Court found that the diversion of trade was caused not by the discrimination in price, but rather by the disinclination of the buyer to lower his prices to match the cuts made by other dealers.

(iii) If a low price is available to buyers from a source other then the seller, we may infer that the competitive injury would result with or without the seller's discriminatory low price. In these circumstances, the seller's price structure cannot be the cause of injury and hence is lawful under the Act.

(d) Product Differentiation. The Courts have recognised that a seller can price a brand-differentiated product at different prices if this differential reflects only the difference in consumer preference. In Borden Co. v. F.T.C., the Fifth Circuit said "competitive injury is not caused by a price differential which measures only the economic value [ie. consumer preference] of a premium label as compared to a private label."

(3) Tertiary Line Competition

The competitive injury clause indicates that tertiary line competition may be examined and, as shall be seen, effects on competition beyond tertiary line may also be examined.


217 For a more detailed discussion of availability see infra, p. 127.

218 Borden Co. v. F.T.C., 381 F.2d 175,180 (5th Cir. 1967), on remand from 383 U.S. 637 (1966).
(a) **Tertiary Line Injury.** The legislative origin of the tertiary level test is obscure\(^{219}\) with Congressional debates concerned only with competitive injury at the primary and secondary lines. Judicial interpretation of tertiary line injury is also sparse with only one case, *Standard Oil Co. v. F.T.C.*\(^{220}\) having sustained a third line price discrimination attack.

Standard Oil, a refiner/supplier, sold gasoline in the Detroit area to both retailers and four jobbers. The 'tank car' prices offered to jobbers were .5 to 1.5 cents per gallon below the 'tank wagon' prices offered to smaller purchasers who sold at retail only. Three of the four jobbers sold at both retail and wholesale levels, (with the majority sales being at wholesale to independent retailers). The fourth jobber sold only at the retail level. The F.T.C. charged that jobbers had passed on some or all of their functional discount to their retailer-customers, giving those retailers a competitive advantage over the retailers who brought at 'tank-wagon' prices from Standard. Thus, competition with a customer of a knowing recipient of a discrimination was impaired.

The F.T.C. Order resulting from the litigation forbade the granting of lower prices to jobbers where the jobbers resold to retailers at lower then 'tank-wagon' prices\(^{221}\). On appeal, the Seventh Circuit stated that no supplier "should....be required to police its wholesalers and sell to them at [its] peril," but should only "be liable if it sells to a wholesaler it knows or ought to have known is engaging

\(^{219}\) Rowe, *op. cit.*, p. 197.

\(^{220}\) *Standard Oil Co., 41 F.T.C. 263 (1945), m'df'd 43 F.T.C. 56 (1946), m'df'd and aff'd 173 F.2d 210 (7th Cir. 1949), rev'd and remanded on other grounds 340 U.S. 231 (1951), m'df'd 49 F.T.C. 923 (1953), rev'd 233 F.2d 649 (7th Cir. 1956), aff'd 355 U.S. 396 (1958).*

\(^{221}\) para. 6 of the Cease and Desist Order, 41 F.T.C. 263 at 285.
in or intends to engage in" the proscribed price cutting\textsuperscript{222}. As Standard did not have, nor could it legally have control over resale prices of jobbers, the Order was confined in such a way that Standard would be guilty only when it passed on a discount knowing that that discount would be passed on to retailer-customers of the jobber\textsuperscript{223}.

The F.T.C. Order, (as amended by the Seventh Circuit), suggests that Standard should supervise the prices at which jobbers resell to retailers. Standard had several alternatives to ensure compliance with the Order. It could deal only with firms from one functional level, or it could sell to firms at both functional levels at the same price\textsuperscript{224}. Alternatively it could attempt to enforce a policy of resale price maintenance either directly, or indirectly by refusing to deal with jobbers that resold at less then the tank-wagon price\textsuperscript{225}. It could adjust the price that it sold to its own retailers to exactly match the price paid by retailers who brought from jobbers\textsuperscript{226}. Finally, it could attempt to match the size of the discount to the amount of savings attributable to dealing with the jobbers and thereby attempt to defend the discount under the cost justification provisions. Each alternative poses difficulties, not the least of which is the possibility of direct conflict with Section 1 of the Sherman Act either because of the RPM or because of collusion between Standard and jobbers to fix the price of gasoline to retailers.

\textsuperscript{222} 173 F.2d at 217.

\textsuperscript{223} id.

\textsuperscript{224} Suggested by the Seventh Circuit in its decision, 173 F.2d at 217.

\textsuperscript{225} Also suggested by the Seventh Circuit, 173 F.2d at 217.

\textsuperscript{226} Although this is almost impossible where there is more then one jobber. Kintner, \textit{op. cit.}, p. 154.
Unfortunately the Supreme Court, in its review of the case, did not examine the implications of the order but reversed the decision on the legal significance of the meeting of competition defence.\footnote{227}

(b) **Beyond the Tertiary Line.** Application of the Act to tertiary line competition has been rare, however, the Supreme Court ruling in \textbf{Perkins v. Standard Oil Co.}\footnote{228} extending the Act to fourth-line injury and beyond, may revitalise the tertiary line provisions.

Perkins, formerly one of the largest wholesalers and retailers in the Pacific Northwest charged Standard Oil Co. of California with a breach of the Act by selling gasoline at lower prices to a competing wholesaler. Standard Oil had sold to Signal Oil & Gas Co., who resold the gasoline to Western Hyway Oil Co., who, in turn, resold it to a retail chain, Regal Stations Co. who competed directly with Perkins. Perkins charged that the discount passed on to Regal had impaired competition to the extent that he had been driven out of business. The case was further complicated in that Regal was a subsidiary of Western Hyway which itself was a subsidiary of Signal.

The Ninth Circuit reversed a jury verdict in favour of Perkins, saying\footnote{229}:

Section 2(a) of the Act, in terms, limits the distributing levels on which a supplier's price discrimination will be recognised as potentially injurious to competition. These are: on the level of the supplier-seller in competition with his own customers; on the level of the supplier-seller's customers; and on the level of customers of customers of the supplier-seller.

\footnote{227} Noting that the result provided under the Robinson-Patman Act may conflict with the policies of the Sherman and Clayton Acts, the Court stated that they "need not now reconcile the Robinson-Patman Act with that of the Sherman and Clayton Acts". S. Ct. at 249 n.15. The three dissenting Justices who would have affirmed the Order, nevertheless suggested that "some amendment might be required in the wording of the order" S. Ct. at 258.


\footnote{229} 396 F.2d at 812 (footnote omitted).
On appeal, Perkins argued that the competitive injury clause contains three distinct tests, with only one of these tests being confined to the tertiary level. The other two tests, those tests carried over from the original Clayton Act, referred to "any line of commerce"; a term that can be applied to any level of competition. Further, the Act would best achieve its broad remedial purposes only if such a wide reading of "any line of commerce" were made. Finally Perkins argued that the action of the subsidiaries Western Hyway and Regal could be attributed to their parent companies thereby reducing the number of functional levels to two or three.

The Supreme Court, in reversing the Ninth Circuit's ruling, went well beyond the contentions made by Perkins. The Supreme Court considered that to confine the Act's application to only three functional levels would be to impose a "wholly ... artifical" limitation which "is completely unwarranted by the language or purpose of the Act."230 Rather the Court applied a broad interpretation to 'customer' in Section 2(a)231, extending it to anyone who sells the supplier's products. Therefore the Act can reach discriminations no matter what level the competitive injury occurs.

(c) Indicia of Injury to Tertiary Line and Beyond. Indicia of third line injury (and beyond) is similar to secondary line. One consideration, however, is whether the recipient of the discrimination must pass on some or all of the discount in order to violate the Act, or whether the mere existence of a differential provides the potential for injury because the discount may be passed on to customers


231 'or with customers of either of them'. The Court noted that this is the same broad interpretation as was given in F.T.C. v Fred Meyer, Inc to the term 'customer' contained in Section 2(d) of the Act. F.T.C. v. Fred Meyer, Inc., 390 U.S. 341 (1968).
of the recipient\textsuperscript{232}. The former view should prevail in treble damages cases because of the need to show actual injury\textsuperscript{233}. Kintner suggests the former view is also appropriate in Government suits because the word "may" used in the Act should be construed to condemn discounts that have been passed on and "may" cause injury\textsuperscript{234}. Indeed, to suggest otherwise would mean to control the profit margins and mark-ups of all middlemen who received a discriminatory discount or condemn any dual-distribution or direct-buying system\textsuperscript{235}.

Rowe provides two further defences to break the causal nexus between the discrimination and tertiary line competitive injury\textsuperscript{236}. First, where the concession passed on by the recipient of the discriminatory discount results from the resale tactics of that distributor then there is no causal link between the seller's discriminatory discount and the distributor's discount. Rowe suggests also that the incompatibility of the Sherman Act with the restrictions on middlemen compelled by the Robinson-Patman Act may provide a defence under the Act.

Finally Rowe states "the premise of the Solicitor General's repudiation of the Standard Oil Co. Order before the Supreme Court in 1957 should discredit all 'third-line' injury Orders as inherently incompatible with antitrust policies"\textsuperscript{237}.

\textsuperscript{232} The F.T.C. Order forbade sales to those jobbers who actually undercut Standards 'tank-wagon' price. Para. 6 of the Cease and Desist Order, 41 F.T.C. 263 at 285.

\textsuperscript{233} Kintner, op. cit., p. 153.

\textsuperscript{234} id.

\textsuperscript{235} Rowe, op. cit., p. 201.

\textsuperscript{236} Rowe, op. cit., p. 203-205.

\textsuperscript{237} Rowe, op. cit., p. 205.
3.15 FUNCTIONAL DISCOUNTS

(1) Introduction

The topic of functional discounts has been delayed until this point, both because of its complicated nature and because it draws upon much of the material just discussed. It is now appropriate to consider legal status of functional discounts. The main rationale for the functional discount is that the discount reflects the cost savings made by a manufacturer when he delegates some of the distribution functions to firms further down the distribution ladder. A related rationale is that by varying the selling price of the goods according to the functional level of the buyer, the seller ensures that there exists competitive equality between all buyers at the same level of distribution. For example, by charging a lower price to a distributor than is charged to a direct-buying retailer, the manufacturer ensures that even after the distributor has added on his own costs (and mark-up), the goods can still be sold to the indirect-buying retailer at a price that is comparable to that paid by the direct-buying retailer.

However, the seller faces considerable difficulties cost-justifying a functional discount, both because the discount often only roughly approximates the cost savings and because the cost-justification defence is difficult to prove. The F.T.C. has also refused to accept that a seller may justify a discount according to the costs incurred by


supra, pp. 23-24.
the buyer in performing distribution functions\(^{240}\). Therefore the legal status of functional discounts more often turns to whether discriminatory prices given to firms operating on a different function levels can harm competition between them.

(2) **Historical Development**

The original Clayton Act did not deal specifically with functional discounts although the F.T.C. did rule on two cases dealing with functional discounts\(^{241}\). In *Mennen Co.*, the F.T.C. issued a Cease and Desist Order preventing Mennen Co., from discriminating between buyers according to their functional class. The Order, however, was reversed on review\(^{242}\) with S. 2 of the Clayton Act deemed to concern only cases where there was injury to primary line competition. Thus the requisite injury to competition was never found. (Only later did the Supreme Court rule that the Section applied to secondary as well as primary line injury).

A second exemption occurred where the seller sold different quantities. Section 2 of the Clayton Act did not apply to 'discrimination in price between purchasers of commodities on account of differences ... [in the] quantity of the commodity sold'. This gave the seller complete discretion to discriminate between buyers who brought in different quantities.

Therefore S. 2 of the original Clayton Act was generally applicable to functional discounts except where:

1) purchasers brought in different quantities of goods, or
2) there was no general competitive effect.

\(^{240}\) *Supra*, pp. 108-110.

\(^{241}\) *South Bead Bait Co.*, 4 F.T.C. 355 (1922); *Mennen Co.*, 4 F.T.C. 258 (1922).

\(^{242}\) *Mennen Co. v. F.T.C.*, 288 F.2d 774 (2d Cir. 1923).
These exemptions were broad enough to allow many functional discounts.

The 1936 Robinson-Patman amendment did not significantly change the legal status of functional discounts from that which prevailed under the original Clayton Act. The authors of the Act explicitly extended the coverage of the Act to include secondary line competition, and the defence of 'differing quantities' was omitted from the new Act.

The original Robinson and Patman bills, as introduced in the Senate and the House, and as reported out by the Senate and House Committees on the Judiciary243 did contain specific authorization of functional discounts. The Patman bill read:

That nothing herein contained shall prevent or require differentials as between purchasers depending solely upon whether they purchase for resale to wholesalers, to retailers, or to consumers, or for use in further manufacture; for the purpose of such classification of customers as wholesalers or jobbers, or retailers, the character of the selling of the purchaser and not the buying shall determine the classification, and any purchaser who, directly or indirectly, through a subsidiary or affiliated concern or broker, does both a wholesale and retail business shall, irrespective of quantity purchased, be classified (1) as a wholesaler on purchases for sale to retail dealers only, not owned or controlled, directly or indirectly, by the purchaser; and (2) as a retailer on purchases for sale to consumers.

This clause sanctioned functional discounts and dealt with the definition of functional class. A buyer was classified according to the level that he sold the goods. This was consistent with the objective of protecting small retailers against large integrated chain stores, yet it had the side-effect of preventing farmers obtaining wholesale prices through their co-operative buying ventures. The section also defined a dual distributor as both a retailer and a wholesaler depending on whether the goods were resold to the final consumer or to a retailer. Thus it condoned charging different prices for the same goods to the

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243 H.R. 8442, 74th Cong., 1st Sess. (June 11, 1935) reported out by the House Committee on the Judiciary March 31, 1936; and S.3154, 74th Cong., 1st Sess, (June 26, 1935), reported out by the Senate Committee of the Judiciary February 3, 1936.
same firm.

Farmers' opposition to the clause resulted in its deletion from both the House and Senate bills\textsuperscript{244}. The final bill, as enacted on June 19, 1936 contained no direct reference to functional discounts.

It seems Congress rejected classifying buyers according to the level at which they brought the goods, (which would have restored wholesaler status to the farmers co-operatives and the integrated chain stores), and sought not to give specific recognition to functional discounts. Further the Robinson-Patman made it more difficult to justify a functional discount, yet Congress noted that an exemption was needed to prevent an alteration of the status of functional discounts under the new Clayton Act\textsuperscript{245}.


The prima-facie view of functional discounts then is simply that there is a price differential between different purchasers and that this is a discrimination in price within the ambit of the Robinson-Patman Act. No clear intention can be discerned from Congressional records.

The legality of functional discounts turns to their impact upon competition. Traditionally competition is viewed between firms competing directly with one another on the same distributive level ie. producers

\textsuperscript{244} The Senate bill, (as reported out by the Senate Committee of the Judiciary), read:
Provided further, That nothing herein contained shall prevent differentials in prices as between purchasers depending solely upon whether they purchase as factors, or wholesalers, or retailers, or consumers or for use in further manufacture...

Senator Vandenberg proposed a broader exemption reinstating 'difference in quantity' as a complete defence against a charge of price discrimination. These would allow discrimination between individual manufacturers as well as discrimination between classes of manufacturers. This exemption was also struck from the bill.

compete with other producers, wholesalers with other wholesalers, and retailers with other retailers. A discrimination between buyers at different functional levels will not injure competition between those buyers because they do not compete between themselves for customers. However, the emergence of dual distribution and direct buying has substantially altered the traditional marketing systems. A functional discount granted to a dual distributor or a direct buyer may impair competition at either or both of the levels of distribution at which that firm operates.

(a) Legal Functional Discount Systems. A seller can adopt a variety of pricing structures which are legal. Where there is no competition between buyers for customers the discrimination will not cause injury to competition. Therefore a differential will be legal if it merely distinguishes between buyers who operate in different geographic or product markets.\footnote{246}{See discussion supra, p. 101-103.}

It is also acceptable for the seller to use a one-price system as in such a case there is no 'discrimination' within the meaning of the Act.\footnote{247}{F.T.C. v. Anheuser Busch, Inc., 363 U.S. 536 (1960). See discussion, supra, p. 70. See also the decision in Bird & Son, Inc., 25 F.T.C. 548 (1937).} Thus a seller may sell to a direct buyer at the same price that he sells to a wholesaler, and the retailers who buy from the wholesaler will have no cause for complaint even though they must buy the goods at a higher price than the direct buyer. The Court considered this problem in Sano Petroleum Corp. v American Oil Co.\footnote{248}{Sano Petroleum Corp. v. American Oil Co., 187 F. Supp. 345 (E.D.N.Y. 1960) at 353-354.}:

Equality in price charged to different purchasers by the same seller is without the ban of Section 2(a) and an injury to competition caused by such equality cannot serve to bring the conduct within the section.
Third, a pricing structure that grants discounts to buyers according to their position in the distribution system will be legal provided the greater discount is granted to buyers higher in the distribution ladder; i.e., the normal functional discount structure is legal. The seller need not attempt to match the size of the discount to the costs of the functions performed by the buyer, the reason being that if a one-price system is legal, then any system more favourable to the higher buyer should also be legal.

(b) **Illegal Functional Discount Systems.** A limitation on the normal functional discount system is when the wholesaler passes on some or all of the functional discount to retailers. In this case the direct buyer is charged a higher price than the retailers who buy from the wholesaler. By examining tertiary line competition the Courts have compared the prices paid by the direct buyer and the indirect buyer and found injury to competition. This factual situation occurred in the important **Standard Oil Co. v. F.T.C. case**\(^\text{249}\). The functional discount system was upheld provided that no jobber undercut Standard's price to direct buyers by passing on some or all of the discount to their retailer-customers.

An alternative to the common form of functional discount is the 'inverted discount' where the buyer who is further down the distribution ladder gets the greater discount. If the direct-buying retailer receives a lower price from the supplier than the wholesaler, then retailers who buy from the wholesaler cannot possibly compete with the direct buyer.

In **Krug v International Telephone & Telegraph Co.**, the District Court found such a pricing policy unlawful notwithstanding the fact that the

\(^{249}\) **Standard Oil Co. v. F.T.C.** 173 F.2d 210 (7th Cir. 1949), rev'd on other grounds 340 U.S. 231 (1951). For a more detailed discussion of the facts and problems relating to the **Standard Oil Co v. F.T.C. case**, see the discussion on tertiary line competition, **supra**, pp. 112-115.
favoured buyer did not compete on the same distributional level as the plaintiff, saying\textsuperscript{250}:

There can be no doubt that a violation of Section 2(a) may occur when a manufacturer sells his products to a retailer at a lower price than that charged to a wholesaler whose customers compete with the retailers.

(c) Determining Functional Class. Much of the difficulty in functional discount cases involves determining the functional 'class' of the buyer. Vertical integration has confused this once easy task with many firms now operating at more than one functional level. The F.T.C., in \textit{Doubleday & Co.}\textsuperscript{251} originally considered functional class to be determined by the purchasers function as a seller and a buyer. However, since \textit{Mueller Co.}\textsuperscript{252}, the Commission has considered functional class to be determined by the level at which the purchaser sells the goods. The direct-buyer therefore has no claim to the wholesaler discount and the seller may charge a higher price to the direct-buyer with almost complete impunity.

Characterization of the buyer according to the level that he resells the goods raises a problem for the dual distributor. As a dual distributor sells at two different levels, he may receive different prices for the same goods. Although an incongruous position, the F.T.C. upheld this in \textit{Standard Oil Co. v. F.T.C.}\textsuperscript{253} The Court condoned the granting of a functional discount on goods resold by jobbers to retailers, however, the jobbers could not receive the discount on goods resold through their own outlets as this would give them a competitive advantage.


\textsuperscript{252} Mueller Co., 60 F.T.C. 120 (1962), \textit{aff'd} 323 F.2d 44 (7th Cir. 1963), \textit{cert. denied} 377 U.S. 923 (1964).

\textsuperscript{253} Standard Oil Co. v. F.T.C., 173 F.2d 210 (7th Cir. 1949), \textit{rev'd on other grounds} 340 U.S. 231 (1951).
advantage over direct-buying retailers who did not receive the wholesalers discount.

One of the difficulties inherent in passing on a discount to a dual distributor is determining what portion of sales are made at each distribution level. In the Sherman Williams Co.\textsuperscript{254} case, the F.T.C. upheld the practice of granting functional discounts to a dual distributor only on goods resold to retailers. However, two subsidiaries of Sherman Williams Co, Lowe Bros. Co. and John Lucas Co. accepted estimates and unverified statements of the portion of goods sold at wholesale level. The statements were often erroneous and overstated and allowed the two firms to pass on a greater discount to their dual distributor clients. The Cease and Desist Order forbade wholesale discounts on any products sold at retail. Thus verification of sales destination is a problem when one applies the Mueller class classification to the dual distributor.

(d) Co-operatives. A consequence of defining class according to the resale function of the buyer is to prevent buyers obtaining wholesaler discounts by establishing co-operatives. Farmers, small independent retailers, etc, are dissuaded from establishing alternative distribution systems that would allow them to compete more effectively with the integrated chain store.

The early co-operative groups, referred to as the 'first generation', were often largely bookkeeping devices for drop shipments and slot shipments to member-buyers and did not perform functions which entitled them to functional discounts. The Courts have examined the wholesaler or co-operative to determine whether it is, in fact, merely an extension of a group of retailers. Where this is so, the members of

\textsuperscript{254} Sherman Williams Co., 36 F.T.C. 25 (1943).
the co-operative are treated as 'Indirect Purchasers' of the supplier and discounts are granted to the buying group according to the distribution level of its members.

The 'second generation' buying groups often performed genuine wholesale functions such as warehousing. Members of these co-operatives have stressed that both the independent nature of the co-operatives and the performance of genuine functions entitles them to a functional discount. The Commission has been unmoved by both arguments and has continued to prevent buying groups being granted functional discounts.

In *F.T.C. v. Alhambra Motor Parts*, the Ninth Circuit remanded the question of whether Alhambra was a separate entity from its members for reconsideration. Alhambra had argued that it had performed legitimate services and was entitled to be treated as a buyer in its own right. On remand, the F.T.C. affirmed its initial view that members of Alhambra were indirect purchasers of the supplier. The significant point about the case, however, is that the Ninth Circuit implicitly suggested by remanding the case that the performance of genuine services may distinguish a legitimate separate entity from an entity that is a mere extension of its members.

Nor has it been accepted that a functional discount is a return for the extra costs incurred when a buyer performs services on behalf of the seller. The seller must justify the discount according to his cost savings and not the extra costs incurred by the buyer. The irrelevance of the internal costs of the buyer has also meant that discrimination is impermissible even when buyers resell the goods by

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different means. Thus a mail-order firm may not receive a discount to compensate him for the greater costs incurred in comparison with a retailer.\footnote{258}

(e) The Indirect Purchaser Doctrine. The Indirect Purchaser doctrine represents an important development in the area of functional discounts. The theory locates an indirect purchaser whenever there exists some relationship between the seller and the eventual purchaser of the goods. This relationship may be found where a RPM agreement exists, or where the seller has some other contact with the purchaser.\footnote{259}

The doctrine was applied in Purolator Products Inc.\footnote{260} Purolator's distribution system is shown in p. 60, Fig. 3.1. The F.T.C. required Purolator to supply to warehouse distributors at the same price as the warehouse distributors sold to affiliated jobbers. This seems to completely ignore that the warehouse distributors were distinct entities who performed genuine functions for which they were entitled to be reimbursed. Clearly a seller cannot afford to maintain close contact with the customers of its buyers. The F.T.C. has intimated that it will apply the Indirect Purchaser doctrine even when the intermediary performs genuine distribution services.

3.16 AVAILABILITY

(1) Availability as a Defence.

Availability has long been recognised as a defence to a charge of

\footnote{258} See Calvani, \textit{op. cit.}, p. 551.
\footnote{259} \textit{Supra}, p. 59.
\footnote{260} Purolator Prod. Inc., 65 F.T.C. 8 (1964), \textit{aff'd} 352 F.2d 874 (7th Cir. 1965).
price discrimination under Section 2(a)\textsuperscript{261}, although it is not explicitly stated in the Act\textsuperscript{262}. The defence is valuable because it provides an alternative to the cost justification provisions. It is often expensive and time consuming to justify volume and quantity discounts, cash discounts, and sales of private label goods by showing that they afford cost savings to the seller, and the cost justification defence often proves a elusive defence. The concept of availability provides a means of avoiding those provisions\textsuperscript{263}.

(2) The Threshold v the Causal Connection Approach to Availability.

The pertinent question to be resolved is at what point in the proceedings should availability be introduced? One commentator suggests that if goods are made equally available to all buyers by the same seller, then the seller is no longer 'discriminating' between buyers and hence there is no discrimination within the meaning of Section 2(a) of the Act\textsuperscript{264}. This accords with the general objective of the Act of achieving fairness and equality between buyers. This approach shall be termed the threshold approach in that availability of the goods by the same seller to all buyers does not give rise to a cognizable discrimination.

The objection to the threshold approach is its inconsistency with

\textsuperscript{261} In the early Kraft-Phenix Cheese Corp., 25 F.T.C. 537 (1937); American Optical Co., 28 F.T.C. 169, 183 (1939); Standard Brands, Inc., 29 F.T.C. 121, 140 (1939); the F.T.C. indicated that the availability of concessions may not give rise to a cognizable discrimination. See Rowe, op. cit., p. 97-98.

\textsuperscript{262} A parallel concept of availability is used in Section 2(d), requiring the provision of services and allowances to be made proportionally 'available' to all buyers. This availability concept has been accepted in Section 2(e) also.


\textsuperscript{264} Rowe, op. cit., p. 93.
the F.T.C. v. Anheuser Busch, Inc. dictum that "a price differential within the meaning of [Section 2(a)]...is merely a price difference"265. The alternative 'causal nexus' approach, consistent with F.T.C. v. Anheuser Busch, Inc., considers the presence of availability as upsetting the causal relationship between the price discrimination and the competitive injury. Since the lower price is available to all buyers, any injury to a buyer is caused not by the discrimination but rather by the buyer's failure to take advantage of the lower price.

The ABA Report isolates the important distinction between the two approaches266:

Unlike the threshold approach which may negate a discrimination at all levels, the nexus approach may have no applicability to primary line discrimination, since competing sellers might still be "injured" by a lost sale at a practically available but discriminatory price.

However, Ira Millstein offers an argument that rationalises the application of the causal nexus approach to both primary and secondary line competition267. Millstein argues that if the seller offers goods at a low price to all buyers then that seller cannot be relying on sales at higher prices to subsidize the low-priced sales, because the seller cannot expect to receive the extra revenue generated by the high-priced sales. Therefore availability destroys the causal nexus between the higher price and the lower price. Millstein adds that if the lower price were universally accepted then competitors of the seller would be hurt more then if the offer were only partially accepted. Since the former case gives rise to no discrimination and is therefore legal, (subject to attack from other antitrust statutes), the latter should also be


267 Millstein, op. cit., pp. 443-444.
considered legal.

The legal status of the threshold and causal nexus approaches is presently unclear. In Universal-Rundle Corp.\textsuperscript{268} the F.T.C. found that a discount for truckload orders was, in fact, not practically available to all purchasers; but, if it were, "it would be difficult to infer competitive injury from...showing that [certain buyers] purchased in small quantities, and at a higher price, then competitors who took advantage of the discount"\textsuperscript{269}. The Commission appears to have accepted the causal nexus view.

Perhaps the most important case to discuss availability was \textbf{F.T.C. v. Borden Co.}\textsuperscript{270} Borden had sold private label milk at prices below its identical brand label product. The F.T.C. had charged Borden with both primary and secondary line injury because of the substantial diversion of trade to Borden from Borden's competitors, and the injury caused to those buyers who still handled Borden's branded product. While not decided on the question of availability, Borden did argue that it would supply private-label milk to any buyer who wanted it and thus the lower priced goods were 'available'. The Supreme Court remanded the case saying\textsuperscript{271}:

\begin{quote}
The Commission will determine, subject to judicial review, whether the differential under attack is discriminatory within the meaning of the Act, whether competition may be injured, and whether the differential is cost-justified or is defensible as a good faith effort to meet the price of a competitor.
\end{quote}

While Justice White's majority opinion is not clear on the question of availability, Justice Stewart, in his dissent, interpretes the majority
It is not clear that the "injury to competition" and "cost justification" issues will be reached on remand. As the opinion of the Court suggests, the existence of price discrimination remains open in the Court of Appeals. If Borden is able to demonstrate that the price differential between the premium and private label brands is not a price discrimination, the inquiry by the Commission is at an end, and no issue of injury to competition or cost justification under S. 2(a) is reached. Nothing in F.T.C. v. Anheuser Busch, Inc., a case concerned only with territorial price discrimination, requires an equation in all circumstances between a price differential and price discrimination. So long as Borden makes private label brands available to all customers of its premium milk, it is unlikely that price discrimination within the meaning of S2(a) can be made out. Boss Mfg. Co. v. Payne Glove Co...

Thus it is not clear whether, as Justice Stewart considers, the majority opinion viewed the presence of availability as preventing a finding of price discrimination, or whether Justice White simply remanded the question of the relation between availability, price discrimination, and injury to competition for consideration by the lower Court.

On remand, the Fifth Circuit thrice stressed that no customer of Borden had ever been denied the right to purchase the lower-priced private brand milk. The Court suggested that injury "may not be the result of the price discrimination but of the buyer's failure to take advantage of the opportunity...to buy at the same prices as other customers." Thus the causal nexus approach seems to have prevailed in this complicated case.

Some Courts have adopted both approaches. In Beam v. Monsanto Co., the Court stated that "there can be no injury to competition" and that "no unlawful discrimination" can occur when a defendant

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272 383 U.S. at 659 n. 17.

273 See Millstein, op. cit., p. 440.

274 Borden Co. v. F.T.C., 381 F.2d 175 (5th Cir. 1967), on remand from 383 U.S. 637 (1966).

asphalt manufacturer made asphalt available on a job-to-job price to all competitors working on a particular project.

(3) Functional Availability

Cases often turn on the question of whether discounts are in fact 'available'. In F.T.C. v. Morton Salt Co., a quantity and volume discount structure was offered to all buyers. However, only five buyers had ever brought in sufficient quantity to qualify for the largest volume discount. The Supreme Court considered that "theoretically, these discounts were available to all, but functionally they were not."\(^{276}\)

In Mueller Co v. F.T.C.\(^{277}\), the Seventh Circuit considered a discriminatory discount offered to 'stocking jobbers' who performed warehousing functions, but not to regular jobbers. While finding in this case, that the discount was not available to all jobbers, the Seventh Circuit implied that a 'practical availability' defence could have been established had the seller demonstrated that the disfavoured buyers were informed of what they must do to obtain the benefit of the discount\(^{278}\). This suggests that a seller may legitimately require a buyer to alter his buying practices in order to take advantage of a discount\(^{279}\).

(4) Availability in Primary-Line Cases.

The Courts have not been so receptive to availability when it relates to primary line cases. The Court in the primary line case Pacific Engineering & Production Co. v. Kerr-McGee Corp., held the


\(^{277}\) Mueller Co. v. F.T.C., 323 F.2d 44 (7th Cir. 1963), cert. denied 377 U.S. 923 (1964).

\(^{278}\) 323 F.2d at 46.

\(^{279}\) Compare Dayton Rubber Co., note 287 and accompanying text.
defence "not legally supportable"\textsuperscript{280}, and in \textit{Continental Baking Co. v.
Old Homestead Bread Co.}, the Tenth Circuit found the defence "peculiarly
inappropriate" in primary line cases\textsuperscript{281}.

(5) \textbf{Availability from Another Source.}

Another consideration is the availability of goods at an equally
low price from another source. It seems universally accepted by
commentators that availability from another source may destroy the
causal nexus between a discrimination and injury to a disfavoured
buyer\textsuperscript{282}. However, availability from another source will not prevent a
finding of primary line injury\textsuperscript{283}.

In \textit{Ark-La-Tex Warehouse Distrib., Inc.},\textsuperscript{284} it was claimed that
an organisation of automotive parts jobbers and twenty two sub-jobber
members violated the buyer-liability provisions of the Robinson-Patman
Act, (section 2(f)), by obtaining jobber prices through their buying
organisation although the sub-jobbers were the real purchasers. The
Commission remanded the case to the Hearing Examiner to determine\textsuperscript{285}:

Whether the alleged price discriminations had the
requisite injurious effect upon competition in the
distribution of automotive parts and, in particular,
whether the non-favoured jobbers were able to purchase
the same products at the prices charged respondents
either from Ark-La-Tex or as a member of it or a similar
group.

\textsuperscript{280} Pacific Engineering & Production Co. v. Kerr-McGee Corp.,
1974-1 Trade Cas. p. 75,054 (D. Utah, 1974), \textit{rev'd on other grounds} 551

\textsuperscript{281} Continental Baking Co. v. Old Homestead Bread Co. 476 F.2d 97
(10th Cir.), \textit{cert. denied} 414 U.S. 975 (1970).

\textsuperscript{282} Rowe, \textit{op. cit.}, p. 186, 193-195; Millstein, \textit{op. cit.}, p. 431;

\textsuperscript{283} Millstein, \textit{op. cit.}, p. 431. ABA Report, p. 113.

\textsuperscript{284} Ark-La-Tex Warehouse Distributors, Inc., Trade Reg. Rep.

\textsuperscript{285} id. at 21312.
The Hearing Examiner found no evidence that jobbers were prevented from joining buying groups or forming their own and concluded that the same goods were available at similar prices from Ark-La-Tex or from another source.\textsuperscript{286}

However, compare this decision to that in \textit{Dayton Rubber Co.}, a case with similar facts as \textit{Ark-La-Tex Warehouse Distributors, Inc.}, but where the F.T.C. stressed that "lower prices are not 'available' where a purchaser must alter his purchasing status before he can receive them".\textsuperscript{287}

Finally, in \textit{Tri-Valley Packing Ass'n v. F.T.C.} the Ninth Circuit discussed availability from another source, saying\textsuperscript{288}:

\begin{quote}
[I]f the lower price would have been available to the nonfavoured buyer in the same market where the favoured buyer made his purchase, the probability of competitive injury due to the fact that the nonfavoured buyer paid more for the product is not the result of price discrimination, but of the nonfavored buyer's failure to take advantage of the opportunity, equally available to him, of buying at the same low prices.
\end{quote}

Unfortunately the Court and F.T.C. on remand, confused the issue of availability from the supplier and availability from another source.

Where goods are available from another source, the goods must be of comparable 'saleability'. In \textit{Purolator Products, Inc. v. F.T.C.}\textsuperscript{289} the Seventh Circuit appeared to recognise that availability to a disfavored buyer of a like product at the same price from another source may disrupt the causal connection between the discriminatory pricing and

\textsuperscript{286} Ark-La-Tex Warehouse Distributors, Inc., F.T.C. Dkt. 7592, at 21, Initial Decision on Remand (F.T.C. 1965).


\textsuperscript{288} Tri-Valley Packing Ass'n v. F.T.C. 329 F.2d 694, 703-704 (9th Cir. 1964).

\textsuperscript{289} Purolator Products, Inc. v. F.T.C., 352 F.2d 874 (7th Cir. 1965).
competitive injury. However, the Court found that a different brand of air filter which did not command the same consumer preference did not constitute an acceptable alternative product\textsuperscript{290}.

3.17 COST JUSTIFICATION

(1) Introduction to the Defences.

Congress did not intend to outlaw all differentials in price nor even all anti-competitive differentials when it enacted the Robinson-Patman Act. A discrimination may be legitimate for reasons other than because it is innocuous to competition. The Act therefore provides three defences, (in addition to the defence of 'availability' implicitly present in the Act), whereby price discrimination may be justified. These defences are the 'cost justification' and 'changing market conditions' defences contained in Section 2(a), and the 'meeting competition' defence contained in Section 2(b).

(2) History and Purpose of the Cost Justification Defence.

The cost justification defence represents recognition by Congress that some methods or quantities of production and distribution may result in lower costs to the seller, and that these cost-savings should be passed on to the buyer (and eventually to the consumer). The favoured buyer is thereby granted a competitive advantage reflecting the greater efficiency of producing and supplying goods to that buyer. The cost justification defence reads:

\textsuperscript{290} 352 F.2d at 882. But see Fowler Mfg. Co. v. H. H. Gorlick, 415 F.2d 1248 (9th Cir. 1969), \textit{cert. denied} 396 U.S. 1012, where the Ninth Circuit rejected the defence that goods that were "standardized as to design, construction and quality, and were of equal 'leader use' were available from another source at an equally low price", (415 F.2d at 1253). In this case however the Ninth Circuit seems to have rejected totally the 'availability from another source' defence in secondary line cases as "[to] hold otherwise would be to make a farce of the Act", (415 F.2d at 1253).
2(a)...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.

The Report of the House Judiciary Committee outlines the purpose of the cost justification provisions as part of the schema of the Robinson-Patman Act:

There is nothing in it to penalize, shackle, or discourage efficiency, or to reward inefficiency. Any physical economies that are to be found in mass buying and distribution, whether by corporate chain, voluntary chain, mail-order house, department store, or by the cooperative grouping of producers, wholesalers, retailers, or distributors - and whether those economies are from more orderly processes of manufacture, or from the elimination of unnecessary salesmen, unnecessary travel expense, unnecessary warehousing, unnecessary truck or other forms of delivery, or other such causes - none of them are in the remotest degree disturbed by this bill. Nor does it in any way infringe the seller's freedom to give a part or all of the benefit of the saving so effected to others with whom he deals, whether in higher prices paid to the producer from whom he buys his raw materials, or in higher wages to those who labor in production or handling of his goods, or in lower prices to the customer, including the ultimate consumer who buys them.

This statement from Representative Utterback defines the scope of the bill:

It is through this clause that the bill assures to the mass distributor, as to everyone else, full protection in the use and rewards of efficient methods in production and distribution in return for depriving him of the right to crush his efficient smaller competitors with the power and resources of mere size. There is no limit to the phases of production, sale, and distribution in which such improvements may be devised and the economies of superior efficiency achieved, nor from which those economies, when demonstrated, may be expressed in price differentials in favor of the particular customers whose distinctive methods of purchase and delivery make them possible.

The cost justification defence is limited in scope by the Quantity Limits Proviso, which reads:


292 80 Cong. Rec. 9417 (1936).
2(a)...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 forgoing shall then not be construed to permit differentials based on differences in quantities greater than those so fixed and established.

This proviso reflects congressional concern that a discriminatory discount resulting from differing quantities (but not methods) of goods purchased, may be of such a magnitude and available to so few buyers that the effect of that discount may be to create a monopoly. Such a differential may be limited, notwithstanding that it can be justified by reference to the lower costs of serving a particular buyer. It was intended that this provision be used carefully:

I do not know at this time of a case anywhere that the language would reach. It may be that there would never be such a case; but what we had in mind in the consideration of this provision was that there might be one concern or two concerns with such purchasing power that they could buy in such tremendous quantities that they would be buying without competition, and that if such an occasion should arise, and the discounts secured by reason of large purchases would tend to promote a monopoly or be unjustly discriminatory, then the Federal Trade Commission, after hearing all parties, should have the power to say, "Above a certain quantity you shall not have any quantity discounts."

The limitation of quantity discounts was the price which consumers must pay if they are to be protected from buyers who, though their tremendous purchasing power, can establish themselves as 'natural monopolies'.

(2) **Burden of Proving Cost-Justification**

The burden of proving that a differential in price is justified by differences in the cost of serving different purchasers rests with

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293 Comments of Senator Logan, 80 Cong. Rec. 6428 (1936).
the seller. This results from a rule of statutory construction, the language of the Act, and the legislative history.

However, where the purchaser is charged with inducing a violation of the Act by receiving a price concession, the onus of proving that the recipient knew or should have known that the differential could not be cost-justified rests with the staff of the Federal Trade Commission. The Federal Trade Commission have greater powers of investigation and disclosure and are therefore better able to obtain the necessary cost data from the seller.

(3) Establishing a Cost-Justification Defence

(a) Determining Price. The price differential to be justified is the difference between the net buying prices of the favoured and disfavoured buyers. Quantity and volume discounts, and cash discounts should be deducted from the invoice price to arrive at the net price. This is identical to the concept used to ascertain the existence of a discrimination in price.

In Sylvania Electrical Products Inc., the issue was the legality of price differentials in the sale of replacement radio tubes.


295 The rule of statutory construction states that the burden of proving a special exception to the prohibition of a statute generally rests on the one who claims the benefits of the exception. Kintner, op cit, p. 161.

296 F.T.C v. Morton Salt Co. The Supreme Court relied on the legislative history and Section 2(b) of the Act to allocate the burden of proof to the seller. Section 2(b) states that "...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".

297 Automatic Canteen Co. v. F.T.C. 346 U.S. 61 (1953); see infra, pp. 179-180.

298 Supra, p. 71.

between Sylvania's own distributors and Philco's marketing organisation. Approximately 600 types of replacement tube were sold by Sylvania, with each buyer generally stocking a complete range. To determine the price paid by distributors for tubes, Sylvania obtained the average price per tube. This was compared with the average price paid by Philco to find the price differential. The Commission accepted Sylvania's price averaging as the disparities between individual tubes were not significant in terms of the inquiry. Sylvania was therefore relieved of the need to justify price differentials on over 600 different items.

(b) **Source of Data.** Much information used in a cost-justification defence can be derived from accounting records although often such records are not maintained in a way totally compatible with the needs of the defence. (For example, the defence requires comparison of the costs of serving individual companies or groups of companies). The time and expense of obtaining cost data is often enormous\(^ {300} \) and for this reason alone the cost justification defence is often viewed as a last ditch attempt to avert a prosecution under the Act.

Although historical (ie. actual or retrospective) costs are to be considered under the Robinson-Patman Act, these costs usually do not form the basis of the original pricing decisions that led to the price differential. Therefore anticipated costs, (for which historical costs are just one of many determining factors), may also be presented to defend a price differential. (Otherwise a seller could only be truly confident that his price differentials reflect cost savings after he verifies all relevant costs - something that the Robinson-Patman Act should not compel).

\(^ {300} \) Herbert Taggart estimates that the initial cost study by Goodrich had taken six men about five or six months, with part-time help from other persons, and that subsequent revisions required at least 495 man-days at a cost probably over $25,000. H.F. Taggart, *Cost Justification*, Ann Arbor: U. Mich. Press, 1955, p. 341,361).
Data may also be gathered using statistical techniques such as sampling, time studies, market surveys, opinions of those experienced in the relevant fields, etc. In *Standard Oil Co.*\(^{301}\) the F.T.C. rejected a sample drawn from Kansas and Oklahoma as unrelated to the cost conditions prevailing in the Detroit area. In *C. E. Niehoff & Co.*\(^{302}\) a sample of 17 customers out of 10,000 was rejected. However, these represent crude uses of statistical techniques and generally the Courts have liberally accepted such attempts to determine costs\(^{303}\).

Rather than attempting to establish cost savings by reference to his own costs, a seller might point to the costs of an independent buyer who has assumed the functions passed on by the seller, claiming that those costs are representative of the costs saved by the seller. No cases have yet considered this point directly. In *Standard Oil Co.*\(^{304}\) Standard attempted to justify a discount to some buyers by showing that these buyers incurred advertising costs, the benefit of which accrued in part to Standard. This was rejected because the costs were those of the buyer and not the seller. Under the competitive injury clause the costs of the buyer have been firmly rejected as irrelevant to the Act. The same approach may be adopted here.

Perhaps the major requirement in developing any cost study is that it be made in 'good faith'. The Advisory Committee recommends that a study made in good faith be given 'great weight' by the F.T.C.\(^{305}\)

(c) Cognizable Costs. The Act requires that the costs differ in

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\(^{301}\) *Standard Oil Co.* (Indiana), 41 F.T.C. 263, 279 (1945).


\(^{303}\) In *U.S. v. Borden Co.*, the Supreme Court noted that "sampling has long been a recognised technique in price discrimination cases". 370 U.S. 460, 466 n. 6 (1962).

\(^{304}\) *Standard Oil Co.* (Indiana) 41 F.T.C. 263 (1945).

"manufacture, sale or delivery resulting from differing methods or quantities at which the goods are to the purchaser sold or delivered". Congressional debates show that the terms "manufacture, sale, or delivery" were not intended to limit the functional areas from which a seller could make and pass on cost-justified discounts. Representative Utterback, after providing examples of "differing methods or quantities" giving rise to cost differences under the proviso, states that such examples were "illustrative of the way in which the bill permits the translation of differences in cost into price differentials as between the customers concerned, no matter where these differences arise". Cost savings that accrue from production, delivery, sale, or any other area may be recognised in price quotations.

However, a seller may only pass on discounts that "result from the differing methods or quantities in which such commodities are to such purchasers sold or delivered". The Chairman of the Conferees explains:

The differential granted a particular customer must be traceable to some difference between him and other particular customers, either in the quantities purchased by them or in the methods by which they are purchased or their delivery taken.

Distinguishing between cost-savings that result from differing 'methods' or 'quantities' is also important as only the latter that can be limited by the Quantity Limits Proviso.

Following some confusion because of the overlap of Section 2(a) and the brokerage section, section 2(c), brokerage has been ruled a legitimate source of cost savings under Section 2(a). The original difficulty arose because it was thought that brokerage should be covered under the stricter per se section which prevents the payment of

306 80 Cong. Rec. 9415 (1936), (emphasis added).

307 80 Cong. Rec. 9417, (emphasis supplied).
brokerage, or discount in lieu thereof, by a seller to a buyer. Nevertheless nothing in Section 2(a) suggests that brokerage is not a legitimate cost. Congress specifically deleted a clause that would have excluded brokerage as a legitimate source of cost savings and discussion at that time indicated that Congress did intend cost savings from brokerage to be passed to the buyer. However it was not clear whether this was to be achieved through Section 2(a) or 2(c). The Supreme Court in *F.T.C. v. Henry Broch & Co.* further confused the issue with the minority opinion accepting that brokerage was a valid cost and the majority rejecting any inferences drawn from the deletion of the brokerage exclusion from the cost justification provisions. In *Thomasville Chair Co. v. F.T.C.* the Fifth Circuit accepted brokerage savings where those savings were passed on to an entire class of buyers and not merely to a single favoured buyer. Section 2(c) was distinguished as preventing the discriminatory payment of brokerage.

The Commission has rejected return on investment as a valid cost. This accepts the accounting concept of cost in preference to the economic concept which would consider the revenue forgone because of the alternative deployment of capital as an 'opportunity cost' of that deployment. In *Thompson Products Co.*, Thompson supplied goods to both wholesalers and vehicle manufacturers. Thompson argued that considerable capital was utilized in buildings, inventory, organization, and credit facilities solely to service one type of customer, the wholesaler.

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310 363 U.S. at 186 n. 11.

311 *Thomasville Chair Co. v. F.T.C.*, 306 F.2d 541 (5th Cir. 1962) at 544-546.

customer. Thompson claimed that this investment ($8,800,000) would ordinarily have netted a return of $166,000.00 and that this amount was a valid cost of dealing with the wholesaler customers. The Commission considered return on investment to be "an allocated portion of the total profits of the company" and "the return rate factor here claimed is thus entirely outside the sphere of actual cost differences"\textsuperscript{313}.

(d) Establishing a Difference in Cost. Congressional debates shed light on how 'differences in cost' between purchasers are to be interpreted. The 'incremental' or 'marginal' cost approach is specifically rejected. According to the House Judiciary Committee, the proviso\textsuperscript{314}:

...precludes differentials based on the imputation of overhead to particular customers, or the exemption of others from it, where such overhead represents facilities or activities inseparable from the seller's business as a whole and not attributable to the business of particular customers concerned in the discrimination.

The Advisory Committee on Cost Justification agrees, saying\textsuperscript{315}:

Cost justification is sometimes claimed solely on the basis of a difference in cost in the seller's entire business with and without the purchases of a particular customer. Such showing should not be considered an appropriate cost-justification device. All customers are entitled to share in the benefits of such a reduction in unit costs, since all customers taking goods from a common source are logically responsible for the effect of volume on unit costs.

Therefore a full-costing approach involving allocations of joint costs and overheads is required. However, a seller need not develop a cost justification defence that allocates all costs incurred by the seller to a buyer. Such full costing far exceeds the requirements of the Act. Rather the Advisory Committee recommends that the study focus

\textsuperscript{313} Thompson Products Co., 55 F.T.C. 1252, 1266, 1276 (1959).

\textsuperscript{314} H.R. Rep. No. 2287, 74th Cong., 2d Sess, 10 (1936).

\textsuperscript{315} Advisory Committee Report, p. 563.
on those costs that "vary either directly or indirectly with the factor upon which the price differential is based"\textsuperscript{316}, and "Areas of cost demonstrably not pertinent to the issues should be excluded from consideration for cost justification purposes"\textsuperscript{317}.

The converse question may also arise: if the seller incurs extra costs in serving the favoured buyer, must he include those costs in an attempt to justify a price differential, or may the cost study only focus on those costs which the favoured buyer has a comparative advantage over the disfavoured buyer? No decision has yet answered this question. Rowe considers that to compel the inclusion of countervailing costs would "complicate and compound the existing difficulties of cost justification" and that "the logic as well as the legislative history of the statutory concept militates against a completely self-defeating compulsion"\textsuperscript{318}. As the Act does not require cost savings to be passed on\textsuperscript{319}, it would seem that even if a disfavoured buyer could show that he had a comparative cost advantage in some areas, there is no compelling reason why a seller should recognize this advantage when calculating the cost savings accrued to the favoured buyer.

\textbf{(e) Allocation of Costs.} Many costs can be identified with particular products, customers, or groups of customers and these direct costs can be readily assigned. A difference in direct costs will usually

\textsuperscript{316} Advisory Committee Report, p. 563.


\textsuperscript{318} Rowe, \textit{op. cit.}, p. 286-287.

\textsuperscript{319} The cost proviso, as reported by the House Judiciary Committee, was phrased as neither preventing or requiring prices which reflect cost economies. H.R. Rep. No. 2287, 74th Cong., 2d Sess. 1,9-10 (1936). The word "require" was deleted as redundant by the Conference Committee. H.R. Rep. No. 2951, 74th Cong., 2d Sess. 6 (1936).
be the easiest cost-savings to identify. Examples include freight charges, advertising to promote branded products, and production costs of particular products.

However, where expenses can be attributable to two or more products, customers, or customer classes, some method must be devised to allocate the expenses. The Advisory Committee suggests the most applicable methods to determine direct costs or to allocate indirect costs are, (in the order listed)\(^{320}\):

1) That method historically used by the company concerned, the result of which has periodically and routinely been evaluated and found reasonably accurate.

2) That method historically used by the company concerned, the result of which has been sporadically evaluated and found reasonably accurate.

3) That method which theoretically appears to be the most logical and reasonable, or that which most closely approximates a satisfactory measure of benefit or activity in terms of rational analysis and can reasonably and practicably be used.

Arbitrary allocations unrelated to the rate at which the cost is incurred will not be accepted. A Court of Appeals stated, "price differentials ought to be justified by concrete and specific cost variances in dealing with different purchasers, and not by conjectural accounting estimates alone"\(^{321}\). A cost study should attempt to allocate costs to the buyers based on the amount of the factor used by each buyer. Time studies and other such techniques may be used to determine the allocation basis.

\(^{320}\) Advisory Committee Report, p. 563.

\(^{321}\) Reid v. Harper & Bros. 235 F.2d 420, 421-422 (2d Cir. 1956). Eg. in Curtiss Candy, the F.T.C. rejected an allocation of joint marketing costs based on the proportionate sales dollar of each customer. 44 F.T.C. 237, 267 (1947).
(f) **Customer Groupings.** The task of allocating costs is eased considerably if the seller is allowed to allocate costs to customer classes rather than on a customer-by-customer basis. Conflicting opinions were given in two Appeal Court cases reviewing the permissibility of group allocations; **American Can Co. v. Bruce's Juices** requiring allocations to be made to individual customers, while in **American Can Co. v. Russellville Canning Co.** allocations to groups of buyers were accepted. Aggregation of customers for cost justification purposes was approved by the Supreme Court in **U.S. v. Borden Co.**

The Commission has continually stressed that the customer groupings must not be too broad as to lose their internal consistency. In **Standard Oil Co.** the Commission considered a price differential between jobbers as one class, and other customers in the Detroit area as a second class. The Commission rejected the second broad classification as failing to distinguish between buyers in suburban and metropolitan areas; the costs of serving suburban areas being higher than the costs of serving the metropolitan area. In **Champion Spark Plug Co.** Champion attempted to justify a special discount granted to two large oil companies. These two purchasers were classified as one group and Champion's other 485 purchasers including other oil companies were combined as a second group. Costs were allocated to each group. The Commission stressed that the second group also included another oil

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company comparable to the two recipients of the discounts and rejected the defence.

Two cases involving the dairy industry bring many issues of customer classification into sharp focus. In Borden Co., Borden established that the average prices paid for private and branded label milk was respectively $5.17 and $6.26 per case. Borden claimed that the $1.09 price differential was more then justified by the $1.27 cost differential between the two brands. The Commission rejected this defence, finding that some customers brought private label milk for as little as $4.89 per case while other customers brought brand label milk for $6.60 per case giving a maximum $1.71 price differential. Thus Borden was faced with justifying price differentials within a class as well as between classes. This is similar to the Thompson Products Co., case where the Commission insisted that a group must consist of homogeneous customers paying similar prices.

The use of broad customer groupings also had difficulties in U.S. v. Borden Co. involving respondents Borden Co. and Bowman Co. Independent stores buying branded milk received certain 'optional customer services' such as moving old milk to the front of the dairy case. Chains did not receive these services and thus the costs of these services were allocated only to independent stores on a volume basis. This customer grouping was rejected as some independents, like chains, did not use these services and therefore should not be allocated part of the cost. In the Supreme Court decision Justice Clark weighted the inexactitudes of customer grouping against the need for practical

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328 Thompson Products, Inc., 55 F.T.C. 1252 (1959). Compare these attempts to average prices over customers with Sylvania's acceptable averaging over product ranges.
standards to govern the cost justification provisions:\(^{329}\):

But this is not to say that price differentials can be justified on the basis of arbitrary classification or even classifications which are representative of a numerical majority of the individual members. At some point practical considerations shade into circumvention of the proviso. A balance is struck by the use of classes for cost justification which are composed of members of such self-sameness as to make the averaging of the cost of dealing with the group a valid and reasonable indicium of the cost of dealing with any specific group member. High on the list of "musts" in the use of average cost of customer groupings under the proviso of Section 2(a) is a close resemblance of the individual members of each group on the essential point or points which determine the costs considered.

Two post-Borden cases indicate that a more liberal approach to customer classification may be taken. The Second Circuit in F.T.C. v. Standard Motor Products, Inc. emphasized that a narrow approach to customer classification may compel the allocation of costs to each buyer; a task so difficult as to remove the cost justification defence as an available defence under the Act. The Court noted that when considering customer classification, the Commission should "reconcile the objectives of the cost justification proviso and the Robinson-Patman Act as a whole"\(^{330}\). In American Motor Corp. v. F.T.C.\(^{331}\) the Sixth Circuit stated that the requisite homogeneity of customers is not dependent on the customers' size or style of doing business "but in the uniformity and 'self-sameness' of American Motors' cost of doing business with them".

Zone pricing, and quantity and volume discounts pose special difficulties for the seller attempting to cost-justify price differentials. Although costs within a zone, or costs of buyers within a particular quantity or volume bracket may be averaged, problems arise


\(^{331}\) American Motor Corp. v. F.T.C., 384 F.2d 247 (6th Cir. 1967).
where two buyers are situated proximately or where two buyers buy in similar quantities or volumes but fall into different brackets. Here averaging techniques may not be accepted because they magnify differences between these buyers and cost justification may be impossible. The question of legality may turn to competitive injury rather than cost justification. If the zone partitions approximate geographic boundaries, or if the quantity and volume brackets are not overly broad and the discounts not overly large, then the pricing system may not cause injury.

(4) "Due Allowance" and the de Minimus Principle

The Act requires only that differentials in price make 'due allowance' for differences in costs. The term 'due allowance' has been used to liberalize the proviso through the introduction of the de minimus principle. Where a cost study fails to justify a differential in its entirety, minor discrepancies may be ignored in an otherwise acceptable cost justification.

The introduction of the de minimus principle results from the admission that a cost study can never exactly justify a differential\(^{332}\):

Cost studies of the sort presented in this manner ordinarily do not afford precise accuracy but must necessarily embrace a number of conjectural factors and allocations. There is inherent in them a reasonable margin of allowable error.

What is this reasonable margin of allowable error? The F.T.C. considered the unjustified residue of a challenged differential in amounts of 0.0064, 0.0047, and 0.0092 cents per dollar of gross sales of rubber and canvas footwear to be de minimi\(^{333}\). In B. F. Goodrich\(^{334}\) the

\(^{332}\) Minneapolis-Honeywell Regulator Co., 44 F.T.C. 351,394 (1948).

\(^{333}\) United States Rubber, 46 F.T.C. 998, 1012 (1950).

Commission accepted a cost justification of all price brackets in a discount structure except one which accounted for less than 1 per cent of total volume of footwear sales. Thus the Commission extended its toleration from infinitesimal disparities between demonstrated costs and challenged price, to entire discount brackets whose total sales volumes were relatively minor in light of potential competitive consequences.  

The acceptability of an unjustified discount may turn on its impact on competition. The rules used to determine secondary line injury are relevant here. In Thompson Products, Inc. the Commission declined to exonerate a residue of about 3 to 7 per cent in an industry "where competition is unusually keen, where margins of profit on individual items are exceedingly small, and where even the 2% cash discount allowed by the respondent is so important to its distributor customers...".

(5) The Quantity Limits Proviso

The quantity limits proviso has been employed (unsuccessfully) on only one occasion to limit quantity discounts in the rubber tyre industry. The Commission had detected "an unmistakable trend of the smaller purchasers towards extinction and of the larger toward monopoly". The Commission sought to halt this trend by limiting the quantity discount available on any one order to 20,000 pounds. The Commission, however, was faulted on review. First because it sought to use the quantity limits proviso to attack the real problem - the huge volumes at which some mass distributors brought. The reference to quantities but not to methods precludes application of the Act to

335 Rowe, op. cit., p. 295.
situations where the buyer's method of purchase affords him the discount. Second the Commission failed to establish the high level of industry concentration required before the proviso could be invoked. These, along with the need to establish procedures and hearings, are the issues still to be resolved by the F.T.C. and Courts\(^\text{339}\).

Finally succinct criticism of the Quantity Limits Proviso was forthcoming from the Attorney General's Committee. This may further add to the demise of the proviso\(^\text{340}\):

We believe that any rational antitrust policy must leave the American business community free to explore new methods of distribution. Arrangements to impede competing distributive techniques have long been viewed as unreasonable restraints of trade. Hence we deplore this singling out and penalizing of the quantity discount system. And while a free economy must place primary reliance on the play of market forces as the determinant of price, the quantity limits proviso, in our view, defeats this policy through ineptly sanctioning a crude form of price-fixing by administrative fiat where competition should safeguard the public interest.

3.18 **THE CHANGING CONDITIONS PROVISO**

The 'changing conditions' proviso in Section 2(a) reads:

2(a) ...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 discontinuance of business in the goods concerned.

The variable saleability of goods is recognised through this proviso. This variable saleability results from 1) changes affecting the market for the goods; and 2) changes in the marketability of the goods. Representative Utterback referred to the proviso as "intended for

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\(^{340}\) Attorney General's Report, p. 177.
protection of purely legitimate trade movements" so as to ensure "liberty of price changes from time to time"\textsuperscript{341}.

(1) \textbf{Changing Conditions Affecting a Market}

Although a complete defence to a charge of price discrimination, the proviso has been employed only rarely by a seller attempting to justify his discriminatory sales. In \textit{Fruitville Canning Co.}\textsuperscript{342}, defendant attempted to show that the rapidly changing conditions affecting prices of canned fruits in the West Coast market justified discriminatory prices favouring direct-buying chains over independents buying through brokers. In rejecting the defence, the F.T.C. found that the price differential was a "customary and normal method of business" and not made in response to "changing conditions"\textsuperscript{343}.

In \textit{Moore v. Mead Service Co.} a predatory price was charged by an inter-state bakery concern to overcome the local boycott of the company's goods. Defendant claimed that the boycott was a "changing condition" in that town justifying the discrimination. The Tenth Circuit found the term "such as" did not limit the section to cases of "actual or imminent deterioration of perishable goods, obsolescence of seasonal goods, distress sales under court process, or sales in good faith discontinuance of business in the goods concerned", but it did limit it to situations of a similar nature\textsuperscript{344}. Changing competitive conditions did not constitute a change in market conditions. In \textit{Balian Ice Cream Co. v. Arden Farms} the Ninth Circuit refused to extend the proviso to exempt price differentials that resulted from differing competitive

\textsuperscript{341} 80 Cong. Rec. 8240–8241 (1936).

\textsuperscript{342} Fruitville Canning Co. 52 F.T.C. 1504 (1956).

\textsuperscript{343} Fruitville Canning Co. 52 F.T.C. 1504, 1515 (1956).

\textsuperscript{344} Moore v. Mead Service Co., 190 F.2d 540, 541 (10th Cir. 1951), \textit{cert. denied}, 342 U.S. 902 (1952).
conditions in the Los Angelos area\textsuperscript{345}.

Thus the proviso may apply where conditions change over \textit{time} but not where they change over geographic areas.

(2) \textbf{Changing Marketability of Goods}

The subsection relating to the "changing conditions in ... the marketability of the goods" has received more favourable acceptance. In \textit{Valley Plymouth v. Studebaker-Packard Corp.}\textsuperscript{346} Studebaker sold over 400 1960 automobiles in late December, (some three months after the release of its 1961 model), at prices 25\% to 30\% lower then charged to the plaintiff. The Court accepted that this price differential resulted from "changing conditions" in the marketability of the goods, basing their result on the facts 1) that the changing conditions exemption was applicable to the manufacturer's lower price on the outdated models; 2) that the overproduction of the 1960 model did not constitute bad faith; and 3) that the sales were made in a bona fide effort to dispose of obsolescent inventory.

In a later case, the Commission distinguished between goods that were 'slow-moving' and goods where there was a 'pronounced and serious deterioration or alteration in the market conditions'; the former deemed insufficient to evoke the "changing conditions" clause\textsuperscript{347}.

\textsuperscript{345} Balian Ice Cream Co. v. Arden Farms 231 F.2d 356,369 (9th Cir. 1955), \textit{cert} denied 350 U.S. 991 (1956).

\textsuperscript{346} Valley Plymouth v. Studebaker-Packard Corp. 219 F.Supp. 608 (S.D. Cal. 1963). See also Peter Satori, Inc. v. Studebaker-Packard Corp., 1964 Trade Case, p.71,309 (S.D.Cal), where the facts and results mirrored the Valley Plymouth v. Studebaker-Packard Corp. case. As both Courts recognised, the jurisdictional elements in both cases may have been missing as there were not at least two \textit{contemporaneous} sales under comparable market conditions.

(3) **Evaluation of the Defence**

There have been insufficient interpretations of the proviso to judge whether it has achieved its intended purpose. Those cases involving 'changing market conditions' seem correctly decided against the seller asserting the defence. The Attorney General's Report considers that the proviso was "designed to promote competitors' freedom to react realistically to the spontaneous movements of a dynamic market" and therefore "a broad interpretation of this provision would, in our opinion, comport best with the Congressional intent as well as broader antitrust objectives"\(^{348}\).

3.19 **MEETING COMPETITION**

(1) **History of the Meeting Competition Defence**

The meeting competition defence contained in Section 2(b) originated from a similar but wider provision contained in the 1914 Clayton Act. Its purpose was to allow a seller whose business extended over a number of geographic areas to lower his price in a single area where he faced competition from a smaller local concern. To prevent this localised meeting of competition would force the larger seller either to forfeit the customers in the local market to the local concern, or to lower his prices in every market in which he sold causing him substantial losses. Second, it would prevent the seller from entering a new market unless he adjusted his prices in all other markets to the level of the new market\(^{349}\). The clause therefore recognises the pro-competitive aspects of price discrimination and the importance of allowing a seller to react to the competitive conditions operating in

\(^{348}\) Attorney General's Report, pp. 178-179.

\(^{349}\) See H.R. Rep. No. 627, 63d Cong. 2d Sess. pt 2 at 2-3 (1914).
each market that he sells. Congressional debates show that the proviso was seen as essentially a truism as a price quoted to 'meet competition' was, in any case, pro-competitive and therefore not proscribed by the 1914 Act.

The commission and courts accepted the defence only where it was used as a defensive counter-measures against the aggressive pricing of a competitor. It could not exempt the seller where predatory intent was found\textsuperscript{350}, where a collusively-adopted pricing systems was adopted\textsuperscript{351}, or where the seller bettered and not merely met the competitor's price\textsuperscript{352}.

The meeting competition defence clause was amended by the Robinson-Patman Act. The House version, which was finally adopted read:

2(b)...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.

The Senate bill which employed the text of the old provision was rejected as "[the] language is found in existing law, and in the opinion of the conferees is one of the obstacles to enforcement of the present Clayton Act"\textsuperscript{353}. The new test was considered narrower than its antecedent\textsuperscript{354}:

This proviso represents a contraction of an exemption now contained in Section 2 of the Clayton Act which permits discriminations without limit where made in good faith to meet competition. It should be noted that while the seller is permitted to meet local competition, it does not permit him to cut local prices until his


\textsuperscript{351} United States Steel Corp., 8 F.T.C. 1,39 (1924).

\textsuperscript{352} Fleischmann Co., 1 F.T.C. 119,134-135 (1918).

\textsuperscript{353} H.R. Rep. 2951, 74th Cong. 2d Sess. 7 (1936).

\textsuperscript{354} H.R. Rep. No. 2287, 74th Cong. 2d Sess. 16 (1936).
competitor has first offered lower prices. If he goes further, he must do so likewise with all his other customers, or make himself liable to all of the penalties of the Act, including treble damages. In other words, the proviso permits the seller to meet the price actually offered by a local competitor. It permits him to go no further.

(2) Meeting Competition as a Complete Defence

The proviso was consistently referred to as "entirely procedural" which "does not set up the meeting of competition as an absolute bar to a charge of discrimination". This direction from Congress fuelled debate when the Commission rejected the proviso as a complete defence in Standard Oil Co., thereby reversing its own stance and taking a view generally at odds with that prevailing in the Appeal Courts. Standard had sold gasoline to jobbers at a lower price to retain their custom in the face of persistent inducements by competitors of Standard.

The Commission had viewed the defence as rebutting a presumption that a differential had injured competition. However, by a positive showing of competitive injury, this presumption of injury was affirmed and an attempt to disprove competitive injury by the meeting competition defence would be of no avail. This 'procedural' interpretation of the Commission makes the proviso redundant for the F.T.C. must prove competitive injury in order to win the case, and thus it matters not whether the defendant succeeds in proving he was merely meeting the competition of another seller.

355 80 Cong. Rec. 9418 (1936), (emphasis supplied).
358 41 F.T.C. 263,281-283 (1945).
On review, the Commission’s interpretation was rejected by the Supreme Court and ‘meeting competition’ was reinstated as a complete defence to a charge of price discrimination. The Court said the proviso, "is readily understandable as simply continuing in effect a defense which is equally absolute, but more limited in scope than that which existed under S. (2) of the original Clayton Act". Legislative intent was dismissed as "inconclusive"; the court preferring to reconcile the intentions of Congress with the objectives of antitrust, saying "Congress did not seek by the Robinson-Patman Act either to abolish competition or so radically to curtail it that a seller would have no substantial right of self-defense against a price raid by a competitor.

(3) Determining "Good Faith" Meeting of Competition

Central to the meeting competition proviso is the concept of 'good faith'. Good faith is necessarily difficult to define although it has been interpreted by the Commission in Continental Baking Co.

At the heart of S. 2(b) is the concept of "good faith". This is a flexible and pragmatic, not technical and doctrinaire, concept. The standard of good faith is

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359 Standard Oil Co. v. F.T.C., 340 U.S. 231 (1951). Because of this interpretation, bills have been introduced to the House and Senate attempting to restore the 'procedural' application employed by the F.T.C. S.11, presented to the Eighty-fourth Congress by Senator Kefauver is representative of these bills. S.11 accepts meeting competition as a complete defence "unless evidence affirmatively shows that the effect of the discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce, in any section of the country".

360 340 U.S. at 251.

361 340 U.S. at 248.

362 340 U.S. at 248,249.

simply the standard of a prudent businessman responding fairly to what he reasonably believes is a situation of competitive necessity. F.T.C. v. A.E. Staley Mfg. Co., 324 U.S. 746,759-60; see Standard Oil Co. v. F.T.C., 340 U.S. 231,249-50. Such a standard, whether it be considered "subjective" or "objective", is inherently ad hoc. Rigid rules and inflexible absolutes are especially inappropriate in dealing with the 2(b) defense; the facts and circumstances of a particular case, not abstract theories or remote conjectures, should govern its interpretation and application.

The Attorney General's Report recommends that the 'good faith' test should "be utilized solely to test the seller's adherence to the basic objectives of the meeting competition proviso: facilitating price reductions in genuine response to competitive market pressures in order to equalize a competitive opportunity" 364.

No hard and fast rules exist for determining "good faith", however, the Courts may consider a number of factors which reflect on the good faith of the businessman. These factors represent the controversial areas of the meeting competition defence.

(4) Beating a Competitor's Price

(a) Meeting the Prices of a Competitor. A seller who adopts an aggressive pricing policy to beat and not merely meet a competitor's price cannot claim 'good faith'. Support for this can be found in the legislative text which refers to meeting an 'equally low' price of a competitor. The Supreme Court in Standard Oil Co. v. F.T.C. declared that Section 2(b) "excludes reductions which undercut" competitive prices 365.

However, the risk of miscalculation because of the difficulty of verifying a competitor's price is not entirely the seller's and some undercutting has been tolerated, as in F.T.C. v. A.E. Staley Mfg. Co.


where the Supreme Court noted that "Section 2(b) does not require the seller to justify price discrimination by showing that in fact he met a competitive price"; rather a seller need show only "the existence of facts which would have lead a reasonable and prudent person to believe that the granting of a lower price would in fact meet the equally low price of a competitor". 

In Samuel H. Moss, Inc. v. F.T.C. the Second Circuit restated the test of meeting but not beating competition: 

...[a seller] could not escape without showing that the offers which it made were either in fact no lower than that of its competitors, or that it did not mean them to be.

(b) Meeting the Price of Goods of Like Fungibility. The products of a competitor need not be of 'like grade and quality' as those of the seller. Where the goods command superior consumer appeal the Commission will consider the value of any premium. In Anheuser Busch, Inc. a seller reduced the price of premium beer in the St. Louis market to match the price of other non-premium beers. The F.T.C. rejected the claim that Anheuser Busch was merely meeting the competitive price:

Budweiser could and did successfully command a premium price in the St. Louis market as it has in most of the other markets in the nation. The test in such a case in not necessarily a difference in quality but the fact that the public is willing to buy the product at a higher price in a normal market. Clearly, therefore, respondent's reduction from the premium price to match the prices of the regional beers on the market was not a meeting of competition. The effect was to undercut competition.

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367 Samuel H. Moss, Inc. v. F.T.C., 155 F.2d 1016 (2d Cir. 1946), at 1016, (emphasis supplied).
368 Anheuser Busch, Inc., 54 F.T.C. 277 (1957), set aside 289 F.2d 835 (7th Cir. 1961).
The Commission allowed the defence in *Beatrice Foods Co.*, accepting that the seller need not exactly match the competitor's price as the seller's brand commanded a premium and the exact value of this premium was unknown\(^{370}\).

The Fifth Circuit in *Callaway Mills Co. v. F.T.C.* further extended the application of the proviso by allowing sellers to meet the prices of any goods of 'equal saleability' and not merely of goods of 'like grade and quality'\(^{371}\). The facts of the case centered around the pricing of tufted carpets by Callaway and Cabin Crafts to meet the competition of other sellers who sold carpet of different quality. The Fifth Circuit, reviewing an F.T.C. decision which stated that the burden of proving the goods of the competitor are of 'like grade and quality' rests with defendant\(^{372}\), preferred to allow the seller to adjust prices not on goods of 'like grade and quality' but on goods of 'equal saleability'\(^{373}\):

The Commission committed error on this point by equating "grade and quality" with "saleability". The two are not synonymous. It is obvious that the consuming public, being far less aware of such factors as "craftsmanship and materials" than professional carpetmakers, cannot easily discern differences in quality between comparable carpeting. Furthermore, the public is greatly influenced by such intangibles as color, design, display, advertising, and similar factors. So long as partitioners conclusively show that their products at various price levels generate public demand (or "saleability") substantially equivalent to that of competitors' carpeting at the same price levels, considerations of "grade and quality" become unnecessary and indeed superfluous, for the most "grade and quality" can do is tend to show "saleability".


\(^{371}\) *Callaway Mills Co. v. F.T.C.*, 362 F.2d 435 (5th Cir. 1966).


\(^{373}\) 362 F.2d at 441.
The 'equal saleability' test has wider application than the 'like grade and quality' test as a seller may meet the prices of a wider range of goods. This should allow the seller greater pricing flexibility.

(5) **Gaining New Customers**

Meeting the inducements of a competitor which are intended to attract a seller's established customers is obviously a defensive pricing policy allowed by the proviso. However, price reductions which net a seller new customers may be interpreted as aggressive pricing and not in good faith. The Supreme Court's 1951 *Standard Oil Co. v. F.T.C.* decision contains numerous references to the statutory authorization permitting a seller "to retain" a customer\(^{374}\). The Court also considered the "actual core" of Section 2(b) the "provision that wherever a lawful lower price of a competitor threatens to deprive a seller of a customer, the seller, to retain that customer, may in good faith meet that lower price"\(^{375}\). These references have been interpreted to mean that a seller may only meet competition to retain an old customer and not to gain new customers.

The problem is especially complex where the seller desires to adopt a pricing system rather than tailor his price reductions to individual competitive situations. In *Standard Motor Products, Inc.* the F.T.C. disapproved of the adoption of a volume discount schedule partly because "the operation of the system was not limited to retaining customers who had been offered a better price"\(^{376}\) but allowed Standard to obtain new customers.

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\(^{375}\) 340 U.S. at 242.

However, there has been some acceptance that 'retaining customers' can also be viewed as retaining a market share or sales volume. More recently in *Sunshine Biscuits, Inc v. F.T.C.* the Seventh Circuit said:

...the distinction between old and new customers is economically unsound and would defeat the purpose of the Robinson-Patman Act. If, in situations where the Section 2(b) proviso is applicable, sellers could grant good faith competitive price reductions only to old customers in order to retain them, competition for new customers would be stifled and monopoly would be fostered. In such situations an established seller would have a monopoly of his customers and a seller entering the market would not be permitted to reduce his prices to compete with his established rivals unless he could do so on a basis such as cost justification. Moreover, the distinction would create a forced price discrimination between a seller's existing customers to whom he had lowered his prices under Section 2(b) and a prospective new customer. These results, we believe, are incompatible with the purpose for which the Robinson-Patman Act was enacted.

The Supreme Court, in *Falls City Industries, Inc v. Vanco Beverage, Inc.*, ended any remaining controversy when it held that Section 2(b) does not distinguish between a seller who meets a competitor's lower price to retain old customers and one who meets a competitor's lower price to gain new customers.

(6) Blanket Price Reductions

A seller may prefer to make general price reductions in an area rather than attempt to target particular buyers. The difficulty of area-wide price reductions is that some buyers in the area may not have been offered the low competitive price. Therefore the seller will be...

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377 Balian Ice Cream 104 F. Supp. 796, 800 (S.D. Cal. 1952), aff'd 231 F.2d 356 (9th Cir. 1955), *cert. denied 350 U.S. 991 (1956).*


undercutting the price to those competitors and no longer meeting
competition in good faith. Because of its indiscriminatory nature, an
area-wide price reduction may also result in an increase in customers.

In Balian Ice Cream Co. v. Arden Farms Co. the Ninth Circuit
suggested a blanket price reduction without needing to identify specific
buyers targeted by the competitor may be permissible\(^\text{380}\). In Forster Mfg.
Co. v. F.T.C.\(^\text{381}\) the First Circuit employed the 'reasonable and prudent'
good faith standard of Staley to allow the seller to evaluate the
competitive necessities of the market without verifying that each
customer in the area was actually offered the competitor's price.

However, excessively broad and drastic price cuts in local areas
to meet the competition of weaker rivals who have made price cuts only
on an individual customer basis will not be accepted as constituting
good faith\(^\text{382}\).

Where a seller can reasonably verify whether each buyer in a
region has been offered a price, the seller has a duty to identify those
buyers and restrict his low price offer only to them. In William Inglis
& Sons Baking Co. v. ITT Continental Baking Co.,\(^\text{383}\) the Ninth Circuit
enunciated a rule based on Staley's 'reasonable and prudent' standard
that "[m]arket wide price reductions are permissible when there is a
reasonable basis to believe that equally low offers are available from
competitors throughout the market", however, given the relative ease of
contacting the small number of buyers in the region to determine

\(^{380}\) Balian Ice Cream Co. v. Arden Farms Co., 231 F.2d 356,358 n.1
(9th Cir. 1955), cert. denied 350 U.S. 991 (1956).

\(^{381}\) Forster Mfg. Co. v. F.T.C., 62 F.T.C 852 (1963), rev'd on
other grounds and remanded 335 F.2d 47 (1st Cir. 1964), cert. denied 380
U.S. 906 (1965).

\(^{382}\) General Gas Corp. v. National Utility, Inc., 271 F.2d 820,825
(5th Cir. 1959).

\(^{383}\) William Inglis & Sons Baking Co. v. ITT Continental Baking
Co., 668 F.2d 1014 (9th Cir. 1981).
whether the competitor's price was in fact offered, the Court found that Continental has failed to discharge its duty of verification.

The most recent consideration of the problem occurred in *Falls City Industries v. Vanco Beverage, Inc.*\(^{384}\) Accepting the legality of area-wide price reductions, the Supreme Court gave conditions that a seller must satisfy in order to meet competition in good faith:

(i) "a seller must limit its lower price to that group of customers reasonably believed to have the lower price available to it from competitors"\(^{385}\);

(ii) the seller must adequately verify the underlying facts on which he reasonably believes that a competitors lower price is available throughout the territory\(^{386}\);

(iii) the lower area-wide price "must continue only so long as the competitive circumstances justifying it, as reasonably known by the seller, persist"\(^{387}\).

The Supreme Court required neither that the competition in the area be very intense\(^{388}\), nor that the area-wide price reduction be the only alternative available to the seller.

(7) *Adopting a Pricing System*

(a) Horizontal Collusion and Reciprocity. As an alternative to meeting the individual prices offered by a competitor, the seller may wish to adopt a pricing system that is employed industry-wide and

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\(^{385}\) 103 S. Ct. at 1296.

\(^{386}\) 103 S. Ct. at 1296.

\(^{387}\) 103 S. Ct. at 1297.

\(^{388}\) A requirement of the Court in *Ballian Ice Cream Co. v. Arden Farms Co.*
thereby meet the competition of all sellers. The use of industry-wide pricing systems is undesirable because it creates pricing inflexibility and could lead to tacit or express collusion between members of the industry.

The difficulty with attacking industry-wide pricing systems such as delivered pricing, quantity and volume discounts, and functional discounts, is that all sellers in the industry can claim they adopted the pricing system to meet the competition of others.

(b) **Rationale For Denying the Defence.** In denying the meeting competition defence to a seller, the Commission has argued that the seller is not responding to a competitor's bid but rather to a pricing system which exists independent of any one competitor.

In **F.T.C. v. A.E. Staley Mfg. Co.** the Supreme Court rejected the adoption of an industry-wide pricing system as the statute "places emphasis on individual competitive situations, rather than upon a general system of competition". In later decisions the Supreme Court refused to sanction the adoption of a collusively-adopted multiple-basing point system, and in **F.T.C. v. National Lead Co.,** a case involving a collusively-adopted zone pricing system, repeated that Section 2(b) was "designed to protect competitors in individual transactions" but did not justify "the use of an entire pricing system".

Three possible interpretations of these cases exist, although analysis is difficult because each case was decided on its special features. As a seller may not collude with others in the industry when setting prices, it may be inferred that collusion is the crucial factor

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390 Cement Institute, 333 U.S. 683, 725 (1948).

reflecting the bad faith of the seller. If this is correct then the relevant line of inquiry is whether the pricing system was adopted by way of collusion, or whether it was adopted merely by parallel action\textsuperscript{392}. However, there was no evidence of collusion in \textit{Staley}.

Alternatively the pricing system, by its very nature, may be illegal and hence a seller may not adopt such a system. This was the interpretation that the Seventh Circuit gave to "\textit{Staley} and kindred cases" when distinguishing \textit{Standard Oil Co. v. F.T.C.}: "the pricing system being illegal, all prices determined thereby were illegal"\textsuperscript{393}. When upholding the functional discount system, the Court accepted the reciprocity argument and deemed it "strange reasoning that one seller should be deprived of the defence provided in S. 2(b) because some other seller might also invoke its protection"\textsuperscript{394}.

Support can also be found in \textit{Staley} and \textit{Cement Institute} for the proposition that a seller is not meeting competition in good faith if the pricing system maintains prices at an arbitrarily high level\textsuperscript{395}. Unfortunately the Supreme Court did not decide these issues in its review of \textit{F.T.C. v. Standard Oil Co.}, but rather found that the F.T.C. had failed to prove that the functional discount system was adopted by \textit{Standard "pursuant to a pricing system" and not in response to}

\textsuperscript{392} See Theatre Enterprises, Inc. v. Paramount Film Distributing Corp., 346 U.S. 537 (1954), which shows the general rule on industry-wide price matching. The Court distinguished between the systems adopted independently or by parallel business behaviour, and systems adopted by express or tacit agreement, only the latter being illegal.

\textsuperscript{393} \textit{Standard Oil Co. v. F.T.C.}, 233 F.2d 649,653 (7th Cir. 1956), (emphasis supplied).

\textsuperscript{394}233 F.2d at 655.

\textsuperscript{395} The Seventh Circuit in \textit{F.T.C. v. Standard Oil Co.}, referred to 'illegal' pricing systems which "stabilize or increase but never lower prices", or that "eliminate all price competition". 233 F.2d 649, 653 (7th Cir. 1956).
individual competitive conditions.\textsuperscript{396}

\textbf{(c) A New Approach to Pricing Systems.} The recent \textit{Callaway Mills Co. v. F.T.C.}\textsuperscript{397} reflects a new acceptance of pricing systems. In that case the Fifth Circuit distinguished \textit{Staley} and, noting that there was nothing wrong \textit{per se} with adopting a pricing system and that there was no "workable alternative" available to Callaway Mills to meet the competition of its competitors\textsuperscript{398}, said\textsuperscript{399}:

\begin{quote}
Under the totality of the circumstances, the discount system, thoughtfully tailored by both petitioners to meet their individual problems in the market, was a mature and reasoned approach to a very real and difficult competitive problem.
\end{quote}

However, the case has not been followed elsewhere. In \textit{Ingram v. Phillips Petroleum Co.} a Federal District Court reverted to the old \textit{Staley} standard\textsuperscript{400}. In \textit{Tri-Valley Packing Ass'n} the F.T.C. did allow a seller to reduce his prices in individual transactions to meet the lower prices of competitors, even though the latter were using a formal pricing system\textsuperscript{401}.

\textbf{(8) Meeting a Lawful Price}

\textbf{(a) Pricing Systems.} The \textit{Staley} case raises the question whether the price met must be a lawful price. The Supreme Court discerned a "clear Congressional purpose not to sanction by \textit{S. 2(b)} the excuse that

\textsuperscript{396} F.T.C. \textit{v. Standard Oil Co.}, 355 U.S. 396 (1958). Both the Court of Appeals and Supreme Court were impressed by the amount of "bargaining and haggling" which was apparent in Standard's pricing. 355 U.S. at 403-404.

\textsuperscript{397} \textit{Callaway Mills Co. v. F.T.C.}, 362 F.2d 435 (5th Cir. 1966).

\textsuperscript{398} 362 F.2d at 441.

\textsuperscript{399} 362 F.2d at 442 (emphasis supplied).


the person charged with a violation of the law was merely adopting a similarly unlawful practice of another. In *Standard Motor Products Inc.*, Standard had offered since 1936 cumulative retroactive volume rebates to each of its jobber customers, as did each of Standard's nineteen competitors. In rejecting the defence, the Commission (upheld by the Courts), stated:

...respondent well knew that the rebates offered by its competitors as well as the rebates offered by respondent to group buyers were unlawful in that the differences in price accorded each group and nongroup purchasers could not be justified by showing differences in the cost of manufacture, sale or delivery since their source is a rebate system, based,...upon combined dollar amount of all sales...

However, in *Callaway Mills Co. v. F.T.C.*[^404^], a case with similar facts to *Standard Motor Products Inc.*, the Fifth Circuit disregarded the issue of the legality of the competitors prices although it was argued by the Commission staff.

(b) **Independent Pricing.** Where an individual competitor's price is illegal the Courts have been reluctant to deny a seller's right to vary his prices to retain customers. In *National Dairy Products Corp. v. F.T.C.* the Seventh Circuit rejected the F.T.C. view that a seller must show circumstances which would lead him to believe the competitor's price was legal[^405^], and reiterated the standard established by the Fifth Circuit in the earlier decision *Standard Oil Co. v. Brown* where the Court said that a seller was only precluded from asserting the 2(b) defence when he is meeting prices "that he knows to be illegal or that


[^404^]: Callaway Mills Co. v. F.T.C., 362 F.2d 453 (5th Cir. 1966).

are of such a nature as to be inherently illegal"406.

Rowe succinctly summarizes the law407:

If a seller's prices merely emulate an actually or inherently illegal pricing system, such as the Chicago-plus formula in the Staley case, the Section 2(b) proviso can furnish no legal succor. If, on the other hand, the lower price is made in a genuine competitive situation, such as prevailing in the Standard Oil controversy, a Section 2(b) defense is not barred so long as the seller could have reasonably believed that the price he was meeting was legal.

(9) Assisting a Buyer to Meet Competition.

The F.T.C. v. Sun Oil Co. case represents the leading case on this question408. Super-Test, a nonmajor supplier, opened a service station across the street from a Sunoco dealer and sold at considerably lower prices than that dealer. Sun Oil reduced its price to the Sunoco dealer allowing him to meet the prices of his competitor. However, Sun Oil did not reduce its price uniformly to its other dealers in the region. The F.T.C. considered Sun Oil's other dealers would be adversely affected by the discriminatory pricing and hence ruled against the reduction409. The Fifth Circuit reversed, viewing the Commission's interpretation as "unnecessarily narrow, unrealistic in terms of the facts of life in marketing gasoline, and inconsistent with the purposes of the Robinson-Patman Act."410. On review, however, the Supreme Court reinstated the F.T.C. decision, interpreting the proviso as concerned with competition between a seller and his rivals and saying Section 2(b) covers only "situations in which the seller reduction in price is made

406 Standard Oil Co. v. Brown, 238 F.2d 54,58 (5th Cir. 1956).
407 Rowe, op. cit., p. 226 (emphasis supplied, footnote omitted).
409 55 F.T.C. at 975-976.
410 Sun Oil Co. v. F.T.C., 294 F.2d 465,471 (5th Cir. 1961), setting aside 55 F.T.C. 955.
in response to a price cut by its own competitor rather than by a competitor of a customer.\footnote{411}

The Court specifically left open the related question of whether the Section 2(b) defence would be available if either the retailer were integrated with the supplier-rival, or the supplier-rival had granted a discount to its retailer.\footnote{412} In its 1967 Report on Anticompetitive Practices in the Marketing of Gasoline the F.T.C. indicated that it would accept the defence if a seller could show that his dealers' competitor had received a comparable price cut from his supplier which was reflected in the competing dealer's retail price.\footnote{413}

(10) \textbf{The Duration of the Price Reduction}

The Commission and Courts have adopted a flexible view on the duration that the seller may offer his price to meet the offer of a competitor. The Supreme Court in \textit{Standard Oil Co. v. F.T.C.} ruled that "continuation of reduction once granted is warranted by S. 2(b) where competitors' reduced price offers are recurring again and again in cutthroat market."\footnote{414} This view has been accepted by the Commission in \textit{C. E. Niehoff & Co.} where the Commission rejected any requirement that a competitive price under Section 2(b) be only temporary.\footnote{415} However, the price reduction should not continue long after the competitor has halted


\footnote{412} The defence was accepted in such a factual situation in Covey Oil Co. v. Continental Oil Co., 340 F.2d 993,997–998 (10th Cir.), cert. denied 380 U.S. 964 (1965).


\footnote{414} \textit{Standard Oil Co. v. F.T.C.}, 355 U.S. at 403 n. 8 (1958).

\footnote{415} \textit{C. E. Niehoff & Co.}, 51 F.T.C. 1114,1130,1146 (1955), aff'd 241 F.2d 37 (7th Cir. 1957), \textit{vacated on other grounds} 355 U.S. 411 (1958).
his inducements.\textsuperscript{416}

(11) **Verification of a Competitor's Price**

The extent that a seller verifies the existence and amount of a competitor's offer and the identity of that competitor may reflect upon his good faith. The Supreme Court in *Staley* referred to the need to show "the existence of facts which would lead a reasonable and prudent business person to believe that the granting of a lower price would in fact meet the equally low price of a competitor."\textsuperscript{417}

(a) **Standards of Verification.** Over the years the standard of verification required by the Commission has lowered in the face of criticism from the Court of Appeals. The Commission was reversed by the First Circuit in *Forster Manufacturing Co. v. F.T.C.* for requiring a seller to show he knew the amount of his competitors' offers and the identity of each competitor who made that offer prior to making his price reduction.\textsuperscript{418} The Fifth Circuit confirmed in *Callaway Mills Co. v. F.T.C.* that the seller need not know the exact price offered on particular products or the particular competitor offering that price.\textsuperscript{419} However, the Commission did affirm in *Exquisite Form Brassiere, Inc.* that a seller should establish those factors which led him to meet his competitors price before he meets that price. An "ex post facto search" will not be accepted as good faith.\textsuperscript{420}

On remand in *Forster Manufacturing Co.* the Commission found that

\textsuperscript{416} International Salt Co., 49 F.T.C. 138, 153 (1952); Champion Spark Plug Co., 50 F.T.C. 30, 42 (1953).


\textsuperscript{418} Forster Mfg. Co. v. F.T.C., 335 F.2d 47, 55-56 (1st Cir. 1964), cert. denied 380 U.S. 906 (1965).

\textsuperscript{419} Callaway Mills Co. v. F.T.C., 362 F.2d 435, 442 (5th Cir. 1966).

Forster had failed to use "due diligence" in verifying competitors prices, Forster merely having accepted statements from buyers that they had received "more interesting offers". In Knoll Associates, Inc. the Commission disallowed the defence where a seller granted discounts of 50% on goods to some department stores who had a policy of buying only at such prices. The Commission considered the Act would be emasculated "if the seller is permitted to discriminate in favor of certain buyers on the mere showing that these buyers insisted on receiving a lower price". And in Viviano Macaroni Co. the Commission considered that the seller need not establish the specific identity of its competitors and the exact amount of the competitors' offers, however, he does have a burden to investigate competitors' offers in order to learn the existence of facts which would lead a reasonable and prudent business person to believe the granting of prices or promotional payments is in response to a genuine offer and does no more than meet that offer. Specifically in the case, the Commission rejected reliance on 'trade experience' to form an opinion as to the identity of a competitor and the use of an 'unlimited offer' to meet the competition.

(b) The 'Lying' Buyer. The difficulty with verification is that the buyer has a pecuniary interest not to reveal the full facts to the seller. As recognised by the First Circuit in Forster Mfg. Co. v. F.T.C.:


The seller wants the highest price he can get and the buyer wants to buy as cheaply as he can, and to achieve their antagonistic ends neither expects the other, 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 of the market place.

One solution to the dilemma of the 'lying buyer' is to attack such buyers under the buyer-liability provisions contained in Section 2(f) of the Act. Previously it was thought that if a seller is exonerated from guilt because he genuinely believed he was meeting a competitor's offer, then the lying-buyer was no longer receiving an illegal discrimination and was therefore also exonerated\textsuperscript{425}. However, the dual cases of \textit{Beatrice Foods, Inc} and \textit{Kroger Co. v. F.T.C.} may give new latitude to attack buyers who induce discriminations by deceptively misrepresenting another seller's bids\textsuperscript{426}. In these cases, the Sixth Circuit sustained the F.T.C.'s decision against the buyer, Kroger Co., even though the F.T.C. had absolved Beatrice Foods of any Section 2(a) violation.

\textbf{(c) Inter-seller Verification.} As an alternative a seller may look to his competitor for confirmation of the offer. However, this may lead to charges of collusion under Section 1 of the Sherman Act and may frustrate the aims of antitrust. The Supreme Court in \textit{U.S. v. Container Corporation of America} condemned an industry-wide agreement to exchange price information concerning sales to specific customers, saying\textsuperscript{427}:

\begin{quote}
The inferences are irresistible that the exchange of pure information has had an anticompetitive effect in the industry, chilling the vigor of price competition... Price is too critical, too sensitive a control to allow it to be used even in an informal manner to restrain competition.
\end{quote}

\textsuperscript{425} See infra, pp. 176, 178.


Later cases seemed to accept the legality of inter-seller verification where it is genuinely conducted to comply with the 'meeting competition' defence\textsuperscript{428}. These cases seem to undercut the \textit{per se} thrust of \textit{Container Corp.}. In \textit{Wall Products Co. v. National Gypsum Co.} the Court allowed such verification as "legitimate practices in furtherance of their obligations to adhere to the requirements of the Robinson-Patman Act and their right to protect themselves against the fraudulent misrepresentations of buyers"\textsuperscript{429}.

However, two recent cases indicate that inter-seller verification may give rise to a complaint under Section 1 of the Sherman Act. In \textit{U.S. v. United States Gypsum Co.} the Court rejected the defendant's "resort to other sellers verification as a means of checking the buyer's reliability" because of Sherman Act prohibition\textsuperscript{430}. The Court indicated that if a seller received similar discounts from other buyers or a threat by the buyer to terminate his purchases, the seller need not further verify the competitor's prices for the purposes of section 2(b).

And in \textit{Great Atlantic and Pacific Tea Co. v. F.T.C.} the Court ruled that for sellers to exchange information would invariably "frustrate competitive bidding and lead to price matching and anticompetitive cooperation among sellers"\textsuperscript{431}. The Court did consider that the threat of

\begin{footnotesize}
\begin{enumerate}
\item \textsuperscript{429} \textit{Walls Products Co. v. National Gypsum Co.}, 324 F. Supp. 295,328 (N.D Cal. 1971).
\item \textsuperscript{430} \textit{U.S. v. United States Gypsum Co.}, 438 U.S. 422,454-455 (1978).
\item \textsuperscript{431} \textit{Great Atlantic and Pacific Tea Co. v. F.T.C.}, 440 U.S. 69,80 (1979).
\end{enumerate}
\end{footnotesize}
loss of an important customer may be sufficient to establish a section 2(b) defence.432

Thus the standards of verification have been relaxed, not because of the need to liberally interpret the meeting competition defence, but because of the need to reconcile the Robinson-Patman Act with broader antitrust objectives.

3.20 BUYER LIABILITY

(1) History and Purpose of the Buyer Liability Section

Paradoxically, although the Robinson-Patman Act was enacted to prevent the abuse of buying power, the Act itself primarily places liability on the seller and provisions extending the Act to buyers were seemingly introduced only as an afterthought. Section 2(f) covers buyer liability and reads:

2(f) That 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.

One important reason why the Act was not primarily aimed at the buyer is because of the Supreme Court's critical approach to government attempts to control distribution channels through the NRA and state price legislation. While controls on sellers were upheld433, bills regulating the price at which buyers purchased the goods were struck down434.

The objective of the Section is outlined by Representative

432 440 U.S. at 84.
The closing paragraph of the Clayton Act amendment, for which section 1 of this bill provides, makes equally liable the person who knowingly induces or receives a discrimination in price prohibited by the amendment. This affords a valuable support to the manufacturer in his efforts to abide by the intent and purpose of the bill. It makes it easier for him to resist the demand for sacrificial price cuts coming from mass-buyer customers, since it enables him to charge them with knowledge of the illegality of the discount, and equal liability for it, by informing them that it is in excess of any differential which his difference in cost would justify as compared with his other customers....This paragraph makes the buyer liable for knowingly inducing or receiving any discrimination in price which is unlawful under the first paragraph of the amendment. That applies both to direct and indirect discrimination; and where, for example, there is discrimination in terms of sale, or in allowances connected or related to the contract of sale, of such a character as to constitute or effect an indirect discrimination in price, the liability for knowingly inducing or receiving such discrimination or allowance is clearly provided for under the later paragraph above referred to.

(2) The Relationship Between 2(a) and 2(f)

The legal liability of the buyer under Section 2(f) is closely related to that of the discriminator under Section 2(a) To establish an illegal discrimination under Section 2(f) all of the jurisdictional elements under 2(a) must be satisfied, there must be injury to competition, and the seller must not be able to successfully invoke any of the statutory defences. In short, a successful prosecution of a buyer requires a concomitant successful prosecution of the seller.

However, Section 2(f) does contain additional jurisdictional elements relating to the 'commerce' requirement and to the knowledge of the buyer and it is useful to outline these, as well as review the

Automatic Canteen Co. v. F.T.C. 436 decision where the Supreme Court

435 80 Cong. Rec. 9419 (June 15, 1936).

outlined the obligations of proof and the allocation of these obligations to the parties involved.

(3) The Commerce Requirement

The text of Section 2(f) demands that the commerce requirements of Section 2(a) be satisfied and, in addition, that the buyer be "engaged in commerce" and the illicit price concession be obtained "in the course of such commerce". While these additional jurisdictional elements may seem to narrow the scope of the Section, the commerce requirements of the antitrust statutes have traditionally been interpreted broadly so as not to restrict their reach. Although there is sparse case history on this subject in relation to Section 2(f), it would seem Courts may continue this broad reading.

To determine whether the buyer is "engaged in commerce" the Courts may consider both the buying and the resale nature of the buyer's business. The requirement may be satisfied if other purchases of the buyer's cross a state line. And even though a sale is made intra-state, the buyer may be considered to have induced a discrimination "in the course of such commerce" because of the inter-state nature of the seller's transaction. In summary, it is unlikely that the additional commerce requirements should significantly restrict the application of the section.

(4) The Buyer's Knowledge

(a) The Automatic Canteen Case. The second additional requirement of 2(f) is that the buyer "knowingly induce or receive a


438 See Rowe, op. cit., p. 437, who quotes Associated Merchandising Corp., 40 F.T.C. 578 (1945) in support.

discrimination in price prohibited by this section" (emphasis added). In the first case concerning this section to be appealed, the Supreme Court dramatically altered the requirements of proof and the allocation of the burden of proof from those which have prevailed under the F.T.C.'s interpretation of the Section. It is useful to examine this case, Automatic Canteen Co. v. F.T.C.\(^{440}\), in some detail.

Automatic Canteen sold candy through vending machines. It had received substantial discounts from its suppliers and this case represented charges against the buyer following successful attacks against the sellers\(^{441}\). In its Initial Decision, the F.T.C. considered that prosecuting staff need show only that the buyer had knowingly received a favourable discount sufficient in size to injury competition. The buyer could then exonerate himself by proving under one of the seller's statutory defences that the discount was legal\(^{442}\). The Court of Appeals concurred, saying the section "places precisely the same burden of proving cost justification upon the buyer, once the Commission establishes knowing inducement or receipt of a price discrimination otherwise illegal\(^{443}\)."

The Supreme Court, however, interpreted the requirements of proof very differently and required proof that the buyer induced or received a discrimination knowing that it was illegal. Thus the F.T.C. must show affirmatively that the discount was illegal and that the buyer knew or should have reasonably known this\(^{444}\). The Court said "the buyer whom


\(^{441}\) Corn Products Refining Co. v. F.T.C., 324 U.S. 726 (1945); Curtiss Candy Co., 44 F.T.C. 237 (1947).

\(^{442}\) Automatic Canteen Co., 46 F.T.C. 361,896 (1950).

\(^{443}\) Automatic Canteen Co. v. F.T.C., 194 F.2d 433,438 (7th Cir. 1952).

\(^{444}\) 346 U.S. at 68,70-71.
Congress in the main sought to reach was the one who, knowing full well that there was little likelihood of a defense for the seller, nevertheless proceeded to exert pressure for lower prices. Enforcement of the provisions of S. 2(f) against such a buyer should not be difficult. 445

(b) Allocation of the Burden of Proof. Since it is more difficult to establish that the buyer knew he was receiving an illegal discount, the Court formulated rules of "convenience" and "fairness" to allocate the burden of proof. The plaintiff retains the burden of establishing the existence of a prima-facie illegal discrimination (i.e. the jurisdictional elements plus injury to competition) 446, and assumes the burden of proving the discrimination was not cost justified 447. The F.T.C. must also show that the recipient knew or should reasonably have known that the discrimination would cause injury to competition and could not be cost-justified.

The size of the discrimination and its systematic nature may allow an inference that the buyer knew or should have known that the discrimination was illegal. According to the Court, the Commission could infer knowledge from the recipient's trade experience and thus the Commission need only show that recipient 448:

...knew that the methods by which he was served and quantities in which he purchased were the same as in the case of his competitor. If the methods or quantities differ, the Commission must only show that such

445 346 U.S. at 79.

446 346 U.S. at 79. The Court also noted that there may be potential conflict between the Sherman and Robinson-Patman Acts if the buyer is allowed to ascertain from the seller whether the discount harms competitors. 346 U.S. at 61,69,74,78.

447 The F.T.C. has broad powers of investigation and subpoena placing it in a better position to obtain the seller's cost data.

448 346 U.S. at 80.
differences could not give rise to sufficient savings in the cost of manufacture, sale or delivery to justify the price differential, and that the buyer, knowing these were the only differences, should have known that they could not give rise to sufficient cost savings. The showing of knowledge, of course, will depend to some extent on the size of the discrepancy between cost differential and price differential, so that the two questions are not isolated. A showing that the cost differences are very small compared with the price differential and could not reasonably have been thought to justify the price difference should be sufficient.

As the buyer has better information on the availability of other sources of supply, the buyer is in a better position to prove that the seller was merely meeting the competition of a rival. Similarly the burden of proving changing conditions rests with the buyer. To ease the evidentiary burden the Supreme Court noted that the F.T.C. may join the seller and buyer in the same proceedings.

(c) Application of the Automatic Canteen Doctrines. Even though the rules of "fairness" and "convenience" were designed to ease the task of prosecution in light of the additional requirements of the Court, the F.T.C. halted enforcement of the Act for several years. The implications of the Automatic Canteen Co. v. F.T.C. case can be seen in cases that occurred upon the resumption of F.T.C. enforcement. In American Motor Specialties v. F.T.C. the Second Circuit considered an F.T.C. Order condemning volume discounts granted to a co-operative association consisting of individual jobbers. These jobbers ordered and received goods separately although the order forms used were those

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449 346 U.S. at 79 n. 23.

450 346 U.S. at 79.

451 Several cases against buyers were dismissed by the F.T.C. shortly after the Automatic Canteen Co. v. F.T.C. decision. Crown Zellerbach Co., 51 F.T.C. 733 (1955); Safeway Stores, Inc., 50 F.T.C. 125 (1953); Kroger Co., 50 F.T.C. 213 (1953); Sylvania Elec. Prods., Inc., 51 F.T.C. 282 (1953).

of the co-operative. The orders of all members of the co-operative were aggregated for the purpose of granting volume discounts. As in all respects except for calculating the discounts, members and non-members brought in the same quantities and dealt with suppliers in the same manner, the Second Circuit confirmed the F.T.C. Order, saying "a member jobber should reasonably have known that the volume discounts could not be justified by the presence of the intermediary co-operative."\textsuperscript{453}

This case may be compared with \textit{Alhambra Motor Parts v. F.T.C.}\textsuperscript{454} where the intermediary co-operative performed legitimate functions. The F.T.C., relying on decisions which place emphasis on the seller's costs and not the buyer's, sought to show that the co-operative members should have known that the existence of the intermediary would not affect the seller's costs. However, no evidence was introduced by the F.T.C. staff to negate a cost justification defence. The Ninth Circuit rejected the F.T.C.'s position and considered that since it was established that there were differences in the method of purchase between members and non-members, the Commission had the burden of showing that these differences in method could not allow cost differentials sufficient in size to justify the discrimination and that the co-operative members knew or reasonably should have known this. On remand the Commission found that the discounts could not be cost-justified and that the buyers did have culpable knowledge of this.

(4) \textbf{Buyer Liability and the Meeting Competition Defence.}

(a) Where the Seller is Precluded from Employing the Defence.

Special problems relate to the meeting competition defence. Where the

\textsuperscript{453} 278 F.2d at 228-229.

seller is, for some reason, prevented from employing the defence, it is unclear whether the buyer is also denied the defence. Although Automatic Canteen Co. v. F.T.C. limits the defences available to the buyer to those available to the seller, strict interpretation of this rule would mean that a buyer violated 2(f) even though he believed the seller was lawfully meeting competition. A more sensible interpretation would be to place upon the F.T.C. staff the burden of showing the buyer knew or reasonably should have known that the seller was not lawfully meeting competition.

(b) Where the Seller is Misled by the Buyer. The converse position may also arise; that is, the seller innocently believes he is meeting the competition of a competitor but his belief is based on incorrect information provided fraudulently by the buyer. Does a failure by the F.T.C. to establish a case against the seller under 2(a) mean that no case can be brought against the buyer under 2(f)? The dual cases of Kroger Co. v. F.T.C. and Beatrice Co.455 dealt with the case of the lying buyer and show that, in such a case, a buyer may successfully be charged with an offence.

A recent case, Great Atlantic & Pacific Tea Co. v. F.T.C.456 was intended to test the legality not of the 'lying buyer', but of the 'silent buyer' - i.e. the buyer who leads the seller into granting excessive discounts but doesn't actually misrepresent his case. Here A & P indicated to Borden that Borden's offer of a discount of $410,000 was "so far out of line it is not even funny" and that a further $50,000 reduction "would not be a drop in the bucket". When Borden doubled its offer, A & P responded saying "Now you're in the ballpark" and accepted


the offer. Nowhere did A & P indicate to Borden that their offer exceeded the competitor's discount of $737,000, although all of A & P's statements were factually correct. The Supreme Court reversed the Second Circuit and upheld A & P's defence that the buyer has no duty under the Act to affirmatively disclose competitor's bids; the Supreme Court's reason for upholding the defence being possible price matching causing conflict between the Robinson-Patman and Sherman Acts. As noted by Mr Justice Marshall in his dissenting opinion, the A & P decision could implicitly reverse Kroger Co. v. F.T.C. and if this is so, enforcement of the good faith meeting of competition provisions will be thwarted. It also appears that even if Kroger Co. v. F.T.C. is not reversed, an inconsistency exists between the cases of the 'lying buyer' and the 'silent buyer' which may allow a buyer to exploit the meeting competition defence to evade the provisions of the Act.

(6) The Status of Buying Corporations and Co-operative Buying Associations

(a) Liability of a Parent for the Purchases of a Subsidiary. Where a subsidiary company purchases the goods, the liability of the parent will be determined by the same standards of domination and participation that normally govern the transfer of liability from one corporation to another. In American News Co., American and its wholly owned subsidiary Union News were held jointly liable for Union's inducement of an illegal promotional allowance.

(b) Co-operative Buying Associations. A co-operative buying association is treated no differently than any other buyer under the Act and Section 4 provides no special privileges other than to allow a co-

operative to distribute its funds to its members:

(4) Nothing in this Act shall prevent a co-operative association from returning to its members, producers, or customers the whole, or any part of, the net earnings or surplus resulting from its trading operations, in proportion to their purchases or sales from, to, or through the association.

The Second Circuit has pointed out that this provision 458:

...does not confer upon co-operative associations any blanket exemption from the Robinson-Patman Act. It only protects a co-operative association from charges of violating the Act premised upon the association's method of distributing earnings...The fact that earnings which result from illegal activity may be distributed to the association's members does not insulate the association from prosecution for the illegal activity. Clearly Section 4 does not permit a co-operative to violate Section 2(f) even though its savings through receipt of discriminatory prices are passed on to its members.

By employing an inverted "Indirect Purchaser" doctrine (the 'buyer corollary' of that doctrine), liability has been placed on the individual members of the co-operative as they control the co-operative's buying activities.

3.21 THE PER SE PROVISIONS

As well as direct and indirect price discrimination, Congress chose to prohibit specific types of indirect discriminations. To this end, Sections 2(c), (d) and (e) were added to the Robinson-Patman Act. Section 2(c) relates to the payment and receipt of brokerage by one side of the sales transaction to the other party. Sections 2(d) and 2(e) relate to the discriminatory granting of promotional services and facilities by sellers to buyers and the discriminatory payment of promotional allowances by sellers to buyers.

These sections are of special interest because of their per se nature. That is, these indirect discriminations are prohibited without

458 American Motor Specialties Co. v. F.T.C. 278 F.2d 225,229 (2d Cir. 1960).
regard to their competitive impact and without provision for justification under the cost justification and meeting competition defences. (Judicial interpretation has written the meeting competition defence into 2(d) and (e)).

There are two explanations for this per se prohibition. The particular practices may be considered by Congress to be incapable of justification and to have such pernicious effects on competition that the competitive injury test is automatically satisfied. The alternative, and more likely reason for applying a stricter test to these practices is to encourage sellers to grant direct rather than indirect discriminations, the former being easier to identify and prevent.

Two problems have occurred because of the distinct tests used for certain indirect discriminations. The first is that it has been difficult to distinguish between discriminations prohibited by Section 2(a) and discriminations prohibited by Sections 2(c), (d), and (e). Second, the Act treats these practices more harshly than necessary. Indeed, 2(c) is far removed from the problem of price discrimination as it does not even require discriminatory dealing. These practices, even when innocuous to competition, are proscribed. Therefore the F.T.C. has had an incentive to bring cases under these sections rather than under Section 2(a).

3.22 THE BROKERAGE PROVISIONS: SECTION 2(c)

(1) Introduction

The brokerage section, S. 2(c) represents the most comprehensive prohibition contained in the Robinson-Patman Act. Its provisions read:

2(c) That 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.

The section is intended to absolutely prohibit the payment or receipt of brokerage by a party on one side of the sales transaction to a party on the other side. The tactic of concealing discounts as a form of brokerage was considered prominent by advocates of the Robinson–Patman Act. This statement by Senator Logan, Chairman of the Subcommittee of the Senate Judiciary Committee outlines the purpose of the section:

459: [T]he bill does not affect legitimate brokerage either directly or indirectly. Where the broker renders service to the buyer or to the seller the bill does not prohibit the payment of brokerage. It is not aimed at the legitimate practice of brokerage, because brokerage is necessary. The broker has a field all his own and he should not be interfered with. In order to evade the provisions of the Clayton Act, however, it was found that while direct price discrimination could not be indulged in, the buyer, if he were sufficiently powerful, could designate someone and say, "That is my broker." Perhaps it was a clerk in his office. Perhaps it was a manager of a store. Perhaps it was a subsidiary corporation organized for the purpose. However, the buyer would say to the seller, "You must sell through that man, and you must pay him a certain percentage or amount of brokerage"; and when the so-called broker or dummy broker received what was paid him, he turned it over to the buyer, and in that way a price discrimination was brought about.

I undertake to say in this august body that there is not a Member of the Senate, there is not a Member of the House, who will not at once condemn a practice of that kind, which provides secret rebates under the guise of brokerage.

The complete prohibition brought about by the section did raise some concern, chiefly among sellers and buyers who did not employ brokers. In response, the cost-justification defence, which had

previously explicitly not recognised brokerage as a legitimate source of cost-savings, was amended to allow sellers to pass on savings in brokerage to buyers in cases where the broker was employed. In addition, co-operatives, fearful that they also would not be granted the cost-savings gained by acting as their own brokers, managed to have the bill amended to allow the payment of brokerage 'for services rendered'.

The effect of these amendments is unclear. Early, narrow rulings effectively prevented the payment of any brokerage to the buyer. These rulings were based on two concepts used in the section. The section is completely self-contained and does not allow a cost-justification defence. Thus 2(a) and 2(c) are not consistent as section 2(a) allows brokerage to be passed on to the buyer as a legitimate cost-saving, while section 2(c) completely prohibits payment of brokerage by the seller to the buyer. Courts preferred to treat brokerage under the specific brokerage section.

The second defect was that the 'for services rendered' provision was undermined by logic such as was expressed in this statement:\footnote{460}{H.R. Rep. No. 2287, 74th Cong., 2d Sess. 15 (1936).}

[T]he positions of buyer and seller are by nature adverse, and it is a contradiction in terms incompatible with his natural function for an intermediary to claim to be rendering services for the seller when he is acting in fact for or under the control of the buyer, and no seller can be expected to pay such an intermediary so controlled for such services unless compelled to do so by coercive influences in compromise of his natural interest.

This statement shows that brokerage can never be paid to the buyer 'for services rendered' because a buyer can never render legitimate brokerage services to a seller. The 'for services rendered' proviso is therefore somewhat of an enigma.

Early rulings showed the section absolutely prohibited the payment of brokerage by one side of the sales transaction to the other.
Those early cases, while not completely discarded, have been mildly disturbed by the Supreme Court's landmark decision in \textit{F.T.C. v. Henry Broch \\& Company}\textsuperscript{461}. While the very specific language of S. 2(c) may prevent a complete judicial overhaul of the section, the \textit{Broch} decision has heralded a more liberal treatment of brokerage discounts.

(2) \textbf{The Prohibitions of 2(c)}.

A careful reading of section 2(c) reveals that it is a relatively simply provision prohibiting the payment or receipt of brokerage or discounts in lieu of brokerage-

(i) by the seller to the buyer,

(ii) by the buyer to the seller,

(iii) by the seller to an agent of the buyer who then passes the discount on to the buyer,

(iv) by the buyer's broker to the seller,

(v) by the seller and the buyer to the same broker.

The tests used to determine whether a broker is an agent of the seller or of the buyer are-

(i) who solicits the services of, and employs the broker,

(ii) in accordance with whose instructions and authorisation does the broker conduct negotiations, and

(iii) whose interests does the broker represent, i.e. whose interests does the broker protect if controversies arise during the course of the sales transactions.

Section 2(c) is self-contained. It contains no references to other sections and, in turn, they do not refer to 2(c). There are seven elements necessary to prove a violation -

1) any person,

2) engaged in commerce, and in the course of such commerce,

3) pays to or receives from,
4) the other party or his agent or representative,
5) anything of value, as a commission, brokerage or discount or allowance in lieu of brokerage,
6) in connection with a sale or purchase,
7) of goods, wares, or merchandise.

Most of the jurisdictional elements are similar to 2(a). The distinctions between the two sections lie in four main areas –
(i) 2(a) requires discriminatory dealing while 2(c) may be violated by a single transaction,
(ii) 2(a) requires a showing of competitive injury, and allows three affirmative defences, whereas 2(c) is violated if brokerage is paid to the other party, with the only exception being 'for services rendered',
(iii) 2(c) contains a test which is symmetrical in its application to the seller and the buyer, whereas the buyer who induces a discriminatory discount is charged under 2(f), where the test of legality differs slightly 462, and
4) the commerce requirement in 2(c) may be wider than the commerce requirement of 2(a) as it may catch export arrangements and intra-state transactions 463.

The most unique result is that 2(c) can be violated by a single transaction and does not require discriminatory dealing. In Jarrett v.

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462 There is no specific 'knowledge' requirement in 2(c) as there is in 2(f). The Supreme Court did indicate that the buyer's knowledge of the form of the discount (ie. whether he believed it was a payment of brokerage or some other form of discrimination), may determine the section under which proceedings are taken. F.T.C. v. Henry Broch & Co., 363 U.S. at 174. See Rowe, op. cit. p. 431.

Pittsburgh Plate Glass Company⁴⁶⁴, Jarrett, an exclusive distributor, brought goods from Pittsburgh Glass on its own account and redistributed them around the country. At the end of each year Pittsburgh paid Jarrett a commission based on volume of sales. This commission was deemed a payment in lieu of brokerage and the arrangement was immediately condemned. The lack of discriminatory dealing or of injury to competition was inconsequential.

(3) Determining Whether a Discount is a Payment of Brokerage

Distinguishing between a payment of brokerage or a discount in lieu of brokerage and an ordinary discriminatory discount covered by 2(a) may be difficult. Congress deliberately employed wide terms to prevent firms circumventing the section. In particular, 2(c) covers "commission, brokerage, or other compensation, or any allowance or discount in lieu thereof". The first step in any investigation is whether either the seller or the buyer deal with a broker. If they do, a discount may be considered a payment of brokerage.

(a) Direct Payments of Brokerage. Brokerage typically comes in the form of bribery, secret rebates, fraudulent receipt of brokerage from both parties to the transaction, commission splitting, etc. Indirect payments of brokerage may be disguised as credits to the buyer, or as discounts from list price such as quantity discounts, functional discounts, etc.

The initial test used to determine if a discount or payment is "in lieu of brokerage" is whether the discount or payment in issue furthers the same purpose and effect as illicit brokerage. Cases where a fee paid to buyers or buyer-controlled brokers is, or once was labelled as 'brokerage' are clearly anticipated by the section and the F.T.C. has

⁴⁶⁴ Jarrett v. Pittsburgh Plate Glass Company, 131 F.2d 674 (5th Cir. 1942).
had little difficulty applying the section to such payments.

An expansive definition of 'brokerage' was used in *Fitch v. Kentucky-Tennessee Light and Power Co.* An employee of a buyer was paid sums of money by a seller to use his influence to persuade the buyer to purchase from the seller. Realising it had been victimised, the buyer commenced charges against the employee, claiming these 'kickbacks' were in lieu of brokerage. The Court agreed that the payments were in lieu of brokerage and paid to the 'other party', and found a violation of 2(c).

(b) Discounts in Lieu of Brokerage. A more confusing situation occurs where it appears that there is some link between brokerage paid to a broker and a price reduction granted to a buyer. The pivot in this analysis seems to be discriminatory payments to brokers and to buyers. A frequent example is where a price reduction to a buyer is given concurrently with a reduction in brokerage to the broker. The test used is whether there is a mathematical equivalence between the discount and the brokerage-saving.

*F.T.C. v. Henry Broch & Co.* is representative of this type of case. Broch was a broker acting on behalf of Canada Foods, Ltd. As Broch performed special services it received a 5 per cent commission; ordinary brokers received a 4 per cent commission. The selling price of the goods, apple concentrate, was set at $1.30 per gallon. Seeking a lower price, J. M. Smucker, a buyer, negotiated with Jensen & Phipps Co., brokers for Canada Foods. Smucker agreed to pay $1.25/g, however, this offer was rejected by Canada Foods, who were prepared to lower their price only after a reduction in brokerage charges. Jensen & Phipps were not prepared to make such a reduction. Learning of the failed


negotiations, Broch approached Smucker and it was agreed between the
parties that Smucker would be given the discount of $0.05/g and Broch
would receive a commission of only 3 per cent.

The F.T.C. initiated an action against Broch, charging it with a
violation of 2(c). The F.T.C. considered the reduction in price to
Smucker and the reduction in brokerage to Broch and concluded that the
discount to Smucker was a payment in lieu of brokerage. The Commission
emphasised that the effect of the deal was the same as if Broch had
directly paid its brokerage to Smucker and this was clearly a violation
of 2(c)467.

The Seventh Circuit reversed this decision for three main
reasons: 1) 2(c) was not intended to cover a seller's independent
broker, 2) the F.T.C. decision encouraged price rigidity by not allowing
brokerage rates to be a variable factor in selling price, and 3) the
case was essentially a private grievance and there was no public
interest involved to justify the Commission's attention to the case468.

The Supreme Court reversed and reinstated the F.T.C. decision by
a 5 to 4 majority, basing their analysis on the need to prevent
circumvention of the section by giving a narrow meaning to the term 'any
person'. In reaching their decision the Supreme Court made this
important statement469:

[N]ot every reduction in price, coupled with a reduction
in brokerage, automatically compels the conclusion that
an allowance in lieu of brokerage has been granted. As
the Commission itself has made clear, whether such a
reduction is tantamount to a discriminatory payment of
brokerage depends upon the circumstances of each case.

468 Henry Broch & Co. v. F.T.C., 261 F.2d 725 (7th Cir. 1958).
469 363 U.S. at 175-176.
The statement recognises that factors other than a decrease in brokerage may give rise to a discount. The most controversial part of the statement, however, is that it seems to require the discriminatory payment of brokerage. The discrimination requirement would be a new jurisdictional element to 2(c) which is not implied by the text of the section. As yet, this requirement has not been accepted by the F.T.C. or the Courts.

(c) Breaking the Presumptive Link Between a Discount and Brokerage. The presumptive link between a reduction in brokerage and a price discount may be broken by a number of factors. In Main Fish Co.,\textsuperscript{470} a wholesaler of fresh fish sold direct to some buyers and through a broker to other buyers. A 5 per cent commission was paid to brokers. In about one third of 52 transactions to a direct purchaser, discounts of 4 to 6 per cent were granted. The Commission did not apply the presumption that these discounts were in lieu of brokerage and instead attributed the discounts to the variable prices of the perishable product. This case is strictly limited to volatile markets.

The presumption was also discarded in Robinson v. Stanley Home Products, Inc.\textsuperscript{471} A seller dismissed all his brokers and proceeded to deal directly with all buyers. It granted a discount to all buyers following the dismissal of the brokers. One of the brokers brought an action claiming that the discount was a payment in lieu of brokerage to buyers. This, of course, was true. Seemingly compelled to find a violation of 2(c), the First Circuit avoided this ludicrous result by establishing a rule that where a seller dismisses all brokers, any subsequent price reduction to buyers must be considered under 2(a).

One feature of the Broch decision is that where a seller can

\textsuperscript{470} Main Fish Co., 53 F.T.C. 88 (1956).

\textsuperscript{471} Robinson v. Stanley Home Products, Inc., 272 F.2d 601 (1st Cir. 1959).
justify a discount from cost-savings other than brokerage, the presumption that a discount is a payment of brokerage will be broken. The question of cost-justification was fully explored in Thomasville Chair Co. v. F.T.C. Thomasville Chair, a manufacturer of household furniture, marketed its products exclusively through a staff of about forty salesmen. These salesmen worked strictly on a commission basis and paid their own expenses including travel. Each had an exclusive geographic area in which they sold. On sales to 'carload' customers, the commission was set at 6 per cent, but on sales to large volume customers, referred to as 'J' customers, the commission was 3 per cent. A 5 per cent reduction off regular price was granted to 'J' customers.

The F.T.C. linked the lower prices to 'J' customers with the reduction in commission and charged a violation of 2(c). At the hearing, Thomasville Chair sought to introduce cost data showing that the discounts could be attributed to cost savings. On an interlocutory appeal, the F.T.C. accepted this evidence was admissible. The Hearing Examiner concluded that the discount was attributable to these other cost-savings and that the discounts were therefore not in lieu of brokerage. On review, the F.T.C. found that the cost-savings from sources other than brokerage did not fully match the discounts, and therefore found it was "conclusively established" that the discounts were partly financed by savings in brokerage and therefore were 'in lieu of brokerage'. The Fifth Circuit reversed and remanded the case for further consideration. Chief among their reasons for remanding the case was a reliance on Broch that a discount derived from cost-savings should not be treated as a payment in lieu of brokerage.

However, the decision by the Fifth Circuit is not fully
consistent with Broch or with the language of 2(c). Broch allowed the presumption between brokerage and a price reduction to be broken if cost-savings occurred in areas other than brokerage and provided these cost-savings were granted to all buyers in a non-discriminatory manner. The Fifth Circuit decision allowed brokerage as a legitimate source of cost-saving.

The link between brokerage and a price reduction is an important part of a case brought under 2(c). There is a presumption that if a price reduction and a brokerage reduction occur reasonably contemporaneously, then the two are connected and the discount is a payment in lieu of brokerage to a buyer. This presumption can only be broken by affirmative evidence to the contrary.

(4) The "For Services Rendered" Exception

(a) The Prohibition on Payments of Brokerage to the Buyer. The "for services rendered" exception found in the section represents one of the mysteries of the Robinson-Patman Act. Although inserted to allow cooperatives to receive brokerage discounts, the House Judiciary clearly noted that it could not be used to allow discounts to be passed on to buyers. This contradictory legislative history has allowed the F.T.C. a free-hand to interpret the exception as it wishes. Accordingly, it has not allowed the payment of brokerage to buyers or to buyer-controlled brokers. A distinct set of cases governing the payment of brokerage by a seller direct to a buyer has developed.

In Biddle Purchasing Co. v. F.T.C.,\(^{473}\) Biddle Purchasing Co., a purchasing company, acted as broker for about 2500 small buyers who paid Biddle according to the services they received. Biddle also received brokerage from sellers which it paid to its retailer-members. The Second

\(^{473}\) Biddle Purchasing Co. v. F.T.C., 96 F.2d 687 (2d Cir.), cert. denied 305 U.S. 634 (1938).
Circuit sustained an F.T.C. Cease and Desist Order, regarding 2(c) as absolutely prohibiting the payment of brokerage to buyers or to buyer-controlled brokers.

(b) Co-operatives and other buyers who render services. This absolute prohibition has caused difficulties when applied to brokers, co-operatives, etc., who genuinely render services to the seller, and also where brokers buy the goods in their capacity as brokers and hence become 'buyers' under the section.

In **Webb-Crawford Co. v. F.T.C.**\(^{474}\), the case of a buyer rendering services was considered by the Fifth Circuit. The Court affirmed the traditional rule that no brokerage payment could be made to a buyer, and, to show this, it went so far as to repunctuate 2(c) so as to limit the 'for services rendered' exception.

However, in the later **Broch** decision, the Supreme Court hinted that where a buyer performed genuine services for the seller, the complete prohibition may not be applicable. In that case, the Court noted there was\(^{475}\):

...no evidence that the buyer rendered any services to the seller or to the [seller's broker] nor that anything in its method of dealing justified its getting a discriminatory price by means of a reduced brokerage charge. We would have quite as different case if there were such evidence and we need not explore the applicability of S. 2(c) to such circumstances.

**Central Retailer-Owned Grocers, Inc. v. F.T.C.**\(^{476}\) was the first case to reconsider the 'for services rendered' provision in light of **Broch**. CROG was a buyer co-operative which received brokerage from the seller and passed it to its members. The F.T.C. applied the old rules

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\(^{474}\) Webb-Crawford Co. v. F.T.C., 109 F.2d 268 (5th Cir. 1940).

\(^{475}\) 363 U.S. at 173.

\(^{476}\) Central Retailer-Owned Grocers, Inc. v F.T.C., 319 F.2d 410 (7th Cir. 1963).
and found a violation of 2(c). The question considered on appeal was whether a discount given to a co-operative should be considered a brokerage payment simply because the co-operative performs the brokerage function. The Seventh Circuit rejected any automatic inference and found that the discount was, in fact, attributable to cost-savings in dealing with the co-operative and was not a payment of brokerage at all. In a later case, the Courts preferred to treat a payment made to buying-brokers as a functional discount rather than as a payment of brokerage.\(^477\)

These cases do not totally resurrect the 'for services rendered' exemption or allow sellers to reimburse buyers for brokerage services performed by the buyer or his agent. However, they do recognise that a seller may grant quantity discounts, promotional allowances, functional discounts, cost-justified discounts, etc, in recognition of other types of services performed by the buyer.

(c) The 'Buying Broker'. The second anomaly occurs where the broker, sensing the opportunity for greater sales, buys the goods in the interim and then resells them. The final effect is usually the same as when a broker acts as agent for the seller, yet the presence of a consummated sale means that the broker becomes the 'buyer' and, as such, may not receive brokerage payments under 2(c). The absolute prohibition has been upheld in these situations, even though such a result may not have been anticipated by Congress.\(^478\)

However, this prohibition was not followed in Hruby Distributing Company.\(^479\). Brokerage was paid to a buying broker who resold solely to wholesalers. This would automatically suggest a violation of 2(c).

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\(^{478}\) Albert W. Sisk & Sons, 31 F.T.C. 1543 (1940).

\(^{479}\) Hruby Distributing Co., 61 F.T.C. 1437 (1962).
However, Commissioner Elman noted that the situation was not one which Congress intended to prevent. Hruby was a strong competitor and a desirable element in the distribution system. Elman emphasized these pro-competitive aspects and declined to find a violation of 2(c).

One area where a prohibition on the payment of brokerage to a buying broker may be justified is where a broker no longer acts merely as a broker, but actually by-passes one of the distribution levels. Such a case is shown in Fig. 3.2.

Fig. 3.2 Distribution Structure Where the Broker By-passes a Functional Level

The buying-broker by-passes the wholesalers and sells direct to retailers. He is then in competition with wholesalers yet he buys at a higher level (by way of his brokerage allowance). Garrett-Holmes & Co., Inc.480 was distinguished from Hruby because Garrett-Holmes resold goods at all levels of distribution, including retailers. A violation of 2(c) was established.

These cases seem to read in a type of competitive injury test into the section in the same way as CROG read in a type of cost-justification defence. This reflects an interesting rejection of the

rigid standards that had earlier prevailed.

(5) Conclusion

Many of the decisions of the F.T.C. and Courts since Broch represent a departure from the severe standards that demand that any payment in lieu of brokerage paid by a seller to a buyer or buyer-controlled broker be found illegal. These new rules have not been crystallized, possibly because they are clearly contrary to the wording of 2(c). Nevertheless, the new directions found in Broch, Thomasville Chair, CROG and Hruby bring a welcome change from the narrow and rigid standards prevailing.

3.23 PROMOTIONAL ALLOWANCES AND SERVICES: SECTIONS 2 (d) AND (e)

(1) Introduction

Congress sought to eliminate discriminations made in the guise of promotional payments\(^{481}\). Buyers had induced such discriminations as an alternative to straight price concessions from seller. Three particular forms of discrimination relating to promotional allowances and services were identified in the Report of the House Judiciary Committee\(^{482}\):

(1) Payments to a customer for promotional services when none were performed.

(2) Payments to a customer greatly in excess of the services actually performed by the customer.

(3) Payments for promotional services to some purchasers while denying promotional assistance to competing purchasers.

The discriminatory granting of services and facilities was condemned because it allowed some buyers to reduce their promotional

\(^{481}\) 80 Cong. Rec. 9418 (1936), Statement of Congressman Utterback.

expenses and increase their sales, thereby giving them a competitive advantage over other competing buyers.

To prevent these discriminations, Sections 2(d) and 2(e) were enacted:

2(d) That 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.

2(e) That it shall be unlawful for any person to discriminate in favour 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 according to all purchasers on proportionally equal terms.

At first glance, these sections contain certain differences which suggest that they require separate analysis: 2(e) is devoid of the interstate commerce requirement of 2(d); 2(d) proscribes discriminatory concessions to competing "customers" while 2(e) encompasses "all purchasers"; 2(d) proscribes payments "for the benefit of" a customer while 2(e) reaches services and facilities furnished to purchasers or contributions thereto; 2(d) requires payments to be "available" on proportionally equal terms whereas under 2(e) services must be "accorded" on this basis; 2(d) simply proscribes disproportionate payments while 2(e) forbids a person to "discriminate" by furnishing disproportionate services or facilities.\(^483\)

\(^{483}\) Rowe, *op. cit.*, p. 390.
However, the Courts have sought to reconcile the differences between the sections as much as possible. The only important remaining distinction is which party performs the promotional services. If they are performed by the buyer, the appropriate section is 2(d); if performed by the seller than proceedings will occur under 2(e).

(2) The Jurisdictional Elements

Most of the 2(d) and (e) jurisdictional elements do not differ significantly from those under Section 2(a). There must be -

(i) two or more contemporaneous consummated sales,
(ii) by the same seller to different purchasers,
(iii) of commodities,
(iv) of like grade and quality,
(v) in interstate commerce.

An 'interstate commerce' requirement does not appear in S. 2(e), however, the Courts have read in a 'commerce' requirement identical to that in S. 2(d). Sections 2(d) and 2(e) (implicitly) prohibit the granting of promotional allowances and services "in the course of commerce", seemingly indicating that the sale to the favoured buyer must occur in commerce. The Courts have not embraced such a restrictive reading and instead merely required that at least one of the sales 'occur in commerce'.

The most significant differences between these sections and 2(a) lie in the areas of refusals to sell and the concept of purchaser.

(3) Determining a Promotional Arrangement

Three separate prerequisites are necessary to establish the existence of a promotional allowance, service or facility caught by 2(d)

485 Eg. see Elizabeth Arden, Inc. v. F.T.C., 156 F.2d 132 (2d Cir. 1946), cert. denied 331 U.S. 806 (1947).
and 2(e) -

(a) a co-operative promotional arrangement,
(b) in connection with a sale,
(c) of goods for resale by the customer.

(a) **Promotional Co-operative Arrangements.** For an allowance or service to be a promotional arrangement under 2(d) and 2(e), it must promote the resale of goods to which it is 'attached'. For example, credit terms granted disproportionately to one buyer will not usually be covered by the section because credit facilities promote the original sale and not the resale of the goods by the buyer to its customers.\textsuperscript{486}

The F.T.C. has outlined a few of the many forms of promotional allowances which might come within 2(d)\textsuperscript{487}. The list is by no means exhaustive. It includes 1) any kind of advertising, 2) handbills, 3) window and floor displays, 4) special sales or promotional efforts for which 'push money' is paid to clerks, salesmen, and other employees of the customer, 5) demonstrators and demonstrations.

An example of the complicated nature of determining a promotional allowance occurred in **State Wholesale Grocers v. Great Atlantic & Pacific Tea Co.**\textsuperscript{488}. There, a seller brought advertising space for its product in *Woman's Day* magazine, a wholly owned subsidiary of A & P. Although the advertising did not promote any particular retail outlet, the magazine was distributed solely through A & P stores. The Seventh Circuit combined the advertising and the restricted distribution of the magazine and found a promotional allowance had been paid to A & P. This

\textsuperscript{486} Eg. Skinner v. U.S. Steel Corp., 233 F.2d 762 (5th Cir. 1946).

\textsuperscript{487} F.T.C., Guides for Advertising Allowances and Other Merchandising Payments and Services. 16 C.R.F. Part 240 (1969), S. 240.5(a).

may be compared with a later decision, where a manufacturer brought advertising space in a magazine owned by the President and controlling shareholder of a customer. No violation was found because the magazine was distributed industry-wide and therefore did not promote the resale of the goods of any one customer.

Determining a promotional service or facility may be even more difficult than determining an allowance as the seller, in his position as packer, deliverer, etc., is in a unique position to offer a variety of promotional services. The F.T.C. has identified common forms of promotional services and facilities: 1) any kind of advertising, 2) catalogues, 3) demonstrators, 4) display and storage cabinets, 5) display materials, 6) special packaging and package sizes, 7) accepting returns for credit, and 8) prizes or merchandise for conducting promotional contests.

As well as attacking promotional allowances and services granted by the seller to the buyer, the F.T.C. has attacked promotional arrangements between the seller and a third party which benefit the buyer. The Intended Benefit Theory was applied to a Tripartite arrangement in the Chain Lightning cases. Certain broadcasting networks had negotiated with retail grocery chains to provide local 'spot' airtime in return for the stores' consent to conduct in-store promotions of products designated by the broadcasting networks. The networks then negotiated with the suppliers of the chains for national

489 NuArc Co. v. F.T.C., 316 F.2d 576, 582 (7th Cir. 1963).

490 F.T.C., Guides for Advertising Allowances and Other Merchandising Payments and Services, S. 240.5(b).

491 This may include providing demonstrators for stores, on-the-job training, provision of trained repairmen, etc.

broadcasting time, using the arrangement with the retailers as an incentive. The Third Circuit considered contracts made between suppliers and networks directly rewarded retailers with spot broadcasting time in exchange for the promotion of the suppliers' products.

Push money, that is, money paid by the seller to employees of the buyer, has been condemned for similar reasons. The employees are treated as independent of the buyer and payments made to them by the seller which benefit the buyer, are seen as promotional services provided by the seller to the buyer through a third party. Interestingly push money has been attacked as a service and facility under 2(e) and as an allowance granted by the seller to the buyer under 2(d).

(b) "in connection with". The promotional arrangement must be "in connection with" sales to a particular customer or group of customers. An interesting situation occurs where a seller provides a particular item from its product line to a buyer while refusing supply to other buyers. If the product has sufficient consumer appeal, then it can be considered as much a promotion as it is a product and in this case, the refusal to supply a product has the same effect as granting a promotional allowance on disproportionate terms.

In the Luxor Ltd. case, the Commission treated the 'junior size' packages of a cosmetic range as 'services and facilities' under S. 2(e) and demanded that they be supplied to all retail outlets which handled the regular sizes. However, this and later cases are considered aberrational and the Courts of Appeal have ruled that the refusal to supply a particular item from a product line cannot be caught under Section 2(e).

493 Luxor Ltd., 31 F.T.C. 658 (1940).
494 See also General Foods Corp., 52 F.T.C. 798 (1956).
This approach treats a promotional product as a product and not as a promotional allowance "in connection with" the sale of other products. As such, a seller may refuse to supply any one item from his line of products. The obvious difficulty with this is that a seller may provide a promotional allowance in the form of a special 'product'.

The right of the seller to advertise his product through any advertising medium is preserved, even if such promotion favours one firm or group of firms, (eg. nation-wide advertising may favour the larger buyers), because the advertising is not connected with particular sales. If the seller does refer to selected customers, then the advertising will be considered a promotional service "in connection with" particular sales to those buyers.

Demonstrating that a promotional arrangement is made "in connection with" particular sales has other complicated dimensions. It requires the promotional arrangement be contemporaneous with sales to particular buyers, or at least, that it occurs within a sufficiently close period of time to indicate that the two are related. In the State Wholesale Grocers v. Great A & P Tea Co. case, a 2(e) violation was rejected as the promotional advertising was "not concurrent with the beginning, or with the ending, of A & P stores' handling of each supplier's products on its shelves"496.

(c) Customer Resale. As the allowance or service must promote the resale of the goods, the goods must be purchased with the intention of resale and a final user cannot be charged with receiving a promotional allowance or service.

Where a buyer handles or converts the goods to another form, the section will still apply. In Corn Products Refining Co. v. P.T.C., the seller, a manufacturer of dextrose, financed an advertising campaign

496 258 P.2d at 837.
which featured the buyer's candy product as "rich in dextrose". The Supreme Court did not consider the substantial conversion of the goods was material, stating "the evils of the discrimination would seem to be the same whether the processing results in little or much alteration of the commodity purchased and resold"497. A parallel argument is applied to goods sold under a private brands. The affixation of the buyer's brand does not alter the purchased product to an extent that the original product is no longer brought for resale.

(4) Determining "Competing Customers"

Promotional arrangements were seen as a form of discrimination induced by large buyers and causing injury to secondary line competition. For this reason S. 2(d) applies where discounts are granted to all "competing customers". A similar requirement has been read into S. 2(e) by the Supreme Court498. This raises two questions: (1) what is a customer for the purposes of 2(d) and (e), and (2) when are customers in competition.

(a) What is a customer? The F.T.C., in their 1960 Guides, saw a customer as either a person who brought direct from the seller, or a person who, by their special relationship with the seller, was considered by law to be a customer, (ie. an Indirect Purchaser)499. This position changed significantly after with the Supreme Court's Fred Meyer Inc. v. F.T.C. decision500. The Supreme Court held that retailer-customers of a wholesaler were also 'customers' of a seller if they

497 Corn Products Refining Co. v. F.T.C., 144 F.2d 211,219 (7th Cir. 1944).
499 F.T.C., Guides for Advertising Allowances and Other Merchandising Payments or Services, 1 CCH Trade Reg. Rep. (1960).
competed with direct-buying retailer-customers of the seller. This new concept of 'customer' is very broad.

(b) What is a Competing Customer? The sections require that customers be in competition. Many of the geographic and customer market dimensions of competition relevant to secondary line injury can be applied here. A seller may discriminate if he confines his promotion to distinct geographic areas or product markets.

The 2(a) concepts of functional competition have been largely discarded after the Fred Meyer case. Even though the terms to a direct-buying retailer and a wholesaler may differ, retailers who buy from the wholesaler will still be considered customers in competition with the direct-buying retailers. In Liggett & Myers Tobacco Co. the Commission found that vending machine operators and wholesalers were not "competing customers" because they operated on different functional levels, however, vending-machine operators and over-the-counter retailers did compete for the same consumer-dollars and were 'competing customers' within the meaning of 2(d) and 2(e).

In general, purchasers will be deemed to be competing customers if they resell at the same functional level and operate in the same geographic and product markets.

(5) Proportionately Equal Terms

The provisions require that promotional allowances and services be granted to purchasers on 'proportionately equal' terms. The onus rests on the seller to establish this equality.

The F.T.C. has accepted that proportionality may be based on

501 See supra, pp. 100-103.

dollar volume or quantity of goods brought in a period of time. It has rejected rates graduated with the volume of business as favouring large buyers. Disparate rates determined by negotiation with individual buyers are also unacceptable. Between these extremes lie a multitude of conceivable bases for calculating proportionate equality. The F.T.C. has indicated that there is no single correct basis for calculating proportionate equality although any formula used should have some relationship to purchaser's volume or promotional contribution.

Rates may be graduated to reflect the quality of the buyer's promotion. This would occur where a seller offers a variety of promotional schemes because a single scheme may not suit particular buyers. For example, a buyer who is too small to undertake a television advertising program may instead be offered the opportunity to advertise in newspapers. In Lever Bros., Inc. the Commission allowed differing rates, accepting the seller's claim that newspaper advertising not only was "more expressive and more effective" but also that "respondents considered it of more value to them and their payments were made on that basis". Where the seller offers a variety of plans, the buyer should be free to choose the plan that best suits his needs.

Where the seller reimburses the buyer for promotional services, the seller has a duty to verify that the services have been performed and the payment is not excessive. This avoids the complaint that payments were made to buyers without a concomitant performance of services. In General Foods Corp., the Commission noted that "there must be a discernable relationship between the amounts paid and the cost or

503 F.T.C., Guides for Advertising Allowances and Other Merchandising Payments and Services, (1969), CRF 240.7.

504 Id.

505 Lever Bros., Inc., 50 F.T.C. 494 (1953), (known as the Soap cases).
reasonable value of the services rendered.\textsuperscript{506}

The standards set in Lever Bros., Inc. best encapsulate the Commission's view on proportionate equality:\textsuperscript{507}

\ldots no standard could be laid down which would insure exact proportionality with the mathematical accuracy of a slide rule,\ldots [however] every plan providing payment for promotional services and facilities should be carefully scrutinized to see that it does conform to the express Congressional intent. It must be honest in its purpose and fair and reasonable in its application.

(6) **Ensuring Promotional Allowances are Available to all Customers**

The provisions require only that all promotional allowances and facilities be made available or accorded to all customers. Availability in the context of promotional allowances means both that the customer must be notified of the promotional plan and that the customer be able to participate in the plan.

(a) **Notification.** A seller must in some way notify a buyer that a promotional allowance or service is available to him. Notification means more than simply making the arrangement available should the buyer wish to participate. It means taking positive action to notify buyers of the scheme. In Vanity Fair Paper Mills, Inc.\textsuperscript{508} the Second Circuit held that a promotional allowance was not available where steps had been taken to conceal it from other buyers. In that case, a standard contract contained a 'Co-operative Advertising Arrangement' clause, however, buyers were not informed that better terms were available on request.

Notification should be in writing if the seller is to completely satisfy the Courts that he has filled his obligation. Buyers should be

\begin{footnotes}
\item[507] Lever Bros., Inc., 50 F.T.C. at 512, (emphasis supplied).
\item[508] Vanity Fair Paper Mills, Inc. v. F.T.C. 311 F.2d 480 (2d Cir. 1962).
\end{footnotes}
notified if the terms change, and, if possible, buyers should be periodically reminded of the existence of the scheme. New buyers should be informed of the scheme as soon as possible and old customers should be given sufficient notice to allow them to take advantage of the scheme. In a situation like that in Fred Meyer, the seller should ensure retailers are properly informed, either by passing on his obligations to the wholesaler, or by direct contact with the retailer, (perhaps by attaching notices to the product itself).

(b) Ability to Take Advantage of an Allowance. Customers must be able to take advantage of an allowance or service. There are two reasons why a buyer may not be functionally able to participate. The activity may be of a type or on a scale that the customer cannot use or afford, or the minimum requirements to qualify for the program are beyond the reach of the particular customer.

The situation in State Wholesale Grocers v. Great Atlantic and Pacific Tea Co. shows a type of promotional arrangement outside the scope of most buyers. A & P operated an exclusive magazine and received promotions through this magazine. The Seventh Circuit ruled that the promotional payments were not functionally available to all buyers because very few retailers had the resources or outlets to sustain a privately distributed magazine. In Elizabeth Arden Sales Corp. v. Gus Blass Co., a demonstrator scheme was functionally available only to larger stores because only they had the turnover necessary to warrant the presence of a demonstrator.

A common way of excluding some buyers is to set minimum requirements on the form or size of the advertising. One reason why a

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seller may do this is to prevent wasteful and ineffective small advertisements. Another reason is simply to exclude smaller buyers. In Exquisite Form Brassiere, Inc.\textsuperscript{511} the seller agreed to reimburse 60 per cent of the cost of any newspaper advertisement that exceeded 400 lines, with no payment for a smaller advertisement. The F.T.C. concluded the scheme was functionally unavailable to all firms too small to feasibly employ newspaper advertising and to all firms too small to reach the minimum requirement.

If a promotional plan is functionally unavailable to some buyers a seller may still justify the plan by showing that alternative acceptable plans are available to those excluded buyers\textsuperscript{512}.

(7) \textbf{Defences to 2(d) and 2(e)}

Sections 2(d) and 2(e) are \textit{per se} offences. Neither the lack of competitive effect nor the cost-justification defence are available to defend a charge of granting discriminatory promotional allowances and services. (Of course, the lack of competitive effect may indicate the customers are not competing, bringing the offence outside the scope of the sections).

The good faith meeting of competition is available under both sections\textsuperscript{513} although its scope is severely limited. Many of the rigidities of this defence have been retained. A seller may meet but not beat competition to preserve existing competition, he must meet a specific competitive offer and cannot meet general industry practices, he must reasonably believe the practice he is meeting is legal, and he must have prior knowledge of the competitive offer. The defence is

\textsuperscript{511} Exquisite Form Brassiere, Inc., F.T.C. Dkt. 6966 (Jan 22, 1960), (Oct 31, 1960).


\textsuperscript{513} Exquisite Form Brassiere v. F.T.C., 301 F.2d 499 (D.C. Cir. 1961), \textit{cert. denied} 369 U.S. 888 (1962).
clearly limited to defensive and not aggressive promotional schemes.

(8) **Buyer Liability**

There is some doubt over the liability under Section 2(f) of buyers who induce or receive promotional allowances that are illegal under Sections 2(d) and (e). This confusion has led to the use of Section 5 of the Federal Trade Commission Act to attack the inducement or receipt of promotional allowances. The F.T.C.'s **Grand Union Co.** decision, approved by the Court of Appeals, is a leading case in this area. Finding the legislative history unclear, the F.T.C. held:

> [I]t is the duty of the Commission to "supplement and bolster" Section 2 of the amended Clayton Act by prohibiting under Section 5 practices which violate the spirit of the amended Act. Consequently, we believe that if a buyer knowingly engages in a course of conduct that accomplishes the result which one of the provisions of the Act is intended to prevent and which Congress has declared to be injurious to competition *per se*, such course of conduct runs counter to the policy of the Act and, as such, is an unfair trade practice within the perview of Section 5 of the Federal Trade Commission Act.

The Commission retained a knowledge requirement parallel to Section 2(f), although they considered the active pursuit by Grand Union of the allowances combined with the exceptional nature of the seller's plan, placed a duty on Grand Union to enquire whether the allowances were proportionally available to other buyers.

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516 F.T.C. Dkt. 6973, pp. 10-11.

517 F.T.C. Dkt. 6973 p. 12. See also the case accompanying Grand News, American News Co. "A buyer who induces a seller to depart from his customary pattern of allowances and grant a promotional payment two or three times greater than previously paid does so at his peril unless possessed of particular knowledge that the seller has granted like concessions to others similarly situated". F.T.C. Dkt. 7396 pp. 8-9 (Jan 10, 1961).
3.24 THE CRIMINAL PROVISIONS: SECTION 3

(1) History and Purpose of the Criminal Provisions

The enactment of criminal provisions as part of the Robinson-Patman Act represents one of the most bizarre episodes in the legislative history of the Act. The criminal provisions, originally known as the Borah-Van Nuys bill after its proponents, Senator Borah and Senator Van Nuys, received support from those fractions who opposed the Robinson and Patman bills. Faced with the inevitable enactment of some form of price discrimination legislation, these fractions saw the criminal nature of the bill and its more restrictive language as limiting its application to price discrimination. It was the lesser of two evils. However, in an unexpected turn-around, criminal provisions similar to the Borah-Van Nuys bill were added to the Robinson bill and contained in Section 3 of the final Robinson-Patman Act.

The purpose of the Borah-Van Nuys bill was to protect competitors from blatant predatory or underhand pricing practices, and to provide a price discrimination statute which, because of its criminal provisions, could be enforced by a local U.S. Attorney, instead of relying on the Washington-based enforcement agencies.

Section 3 reads:

(3) 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, 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

518 S. 4171.

519 See generally 80 Cong. Rec. 6336-6339 (April 29, 1936).
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 $5000 or imprisoned not more than one year, or both.

(2) **Structure of Section 3**

Section 3 contains three separate prohibitions -

(a) discrimination between competing purchasers,

(b) geographic price discrimination,

(c) sales at unreasonably low prices.

Section 3 largely duplicates and overlaps Section 2(a) and activity caught under 2(a) may also violate S. 3. However, there are some differences between the two sections which should be noted.

Section 3 refers to 'Any person'. This term encompasses only the seller and possibly his agent. This can be seen from the language of the section which makes liable the person who engages in geographic price discrimination or sales at unreasonably low prices, and which places 'Any person' in juxtaposition with the 'purchaser'. The Justice Dept. has recognised that 'Any person' must be a seller by confining its litigation to sellers.

The jurisdiction element of a consummated sale found in 2(a) is replaced with a wider test in S. 3 which encompasses executed and executory contracts. S. 3 applies to any 'contract to sell'.

(3) **The Prohibitions of Section 3**

(a) **Discrimination between purchasers.** Section 3 prohibits a seller from granting a discriminatory discount, allowance, or advertising service charge over and above what is available to other

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competing purchasers of goods of like grade, quality, and quantity. The term 'knowing' indicates that the seller must be conscious that he is discriminating between purchasers. Thus, although the section does not contain the defences found in Sections 2(a) and 2(b), if a seller could successfully invoke one of these defences, then he no longer knowingly discriminates between purchasers. These defences therefore become relevant when determining the seller's knowledge.

In addition to a 'knowledge' requirement, it must be shown that the discounts were not 'available' to competing purchasers. This does not mean that a seller must advertise the availability of the discounts. Rather it demands an active refusal by the seller to supply goods on the same terms. The section has been interpreted to condemn only secret or fraudulent concessions and does not extend to published discriminations. The 'knowledge', 'availability', and 'secrecy' requirements will probably be satisfied if the seller consciously tries to conceal discounts.

A 'purchaser' in this part of S. 3 has not been given the same wide meaning as was given in Fred Meyer, Co. v. FTC521. Instead it is taken to mean a person who purchases the goods direct from the seller522.

An additional limitation on S. 3 is that the disadvantaged purchaser must buy in the same quantity as the advantaged purchaser. It is disputable when quantity differences become so significant as to prevent the application of the section. Unfortunately no cases have been decided to clarify this issue.

(b) Geographic Price Discrimination. There is provision in the


section for a ban on geographic price discrimination motivated by a desire to destroy a competitor. There are two distinct elements to be proven:

1) there must be sales in selected geographic areas at prices lower than those in other areas, and

2) the seller must undertake such geographic price discrimination for the purpose of destroying a competitor.

Predatory intent may be found from direct evidence or inferred by circumstances surrounding the discriminatory pricing. The seller may show that he did not intend to destroy a competitor by establishing that the predatory discrimination was motivated by some other reason, such as to meet competition, to meet differing conditions in a market, to sell obsolete or deteriorating goods, to promote a new product, or to retain his market share.

The distinction between 2(a) and this part of S. 3 may be more semantic than real in primary line cases. A showing of primary line injury under 2(a) requires evidence of predatory intent (Utah Pie aside). Thus the standards are very similar under the two sections.

(c) Sales at Unreasonably Low Prices. This prohibition was inserted to prevent blanket price cuts and the excessive use of loss-leaders, especially of popular well-accepted brands, employed for the purpose of eliminating a competitor. There are two elements in a violation:

(i) the seller must make sales at unreasonably low prices, defined as below some level of cost, and

(ii) the sales must be made for the purpose of eliminating a competitor.

The meaning of 'unreasonably low' was discussed in F & A Ice
Cream Co. v. Arden Farms Co. 523:

Whether a price is high or low, and if so, whether it is unreasonably so, can be determined by ordinary business and accountancy methods which take into consideration cost, market, usual profits and other elements. The unreasonably low price which the statute considers an evil would rarely, if ever, be an initial price, except in the rare instance where it would relate to a product not previously marketed. In most instances, it would involve a sudden and unexpected change of price in a staple article of commerce by one engaged in a competitive field. So, in determining its character, and whether it was put into effect as a means of destroying competition, additional elements...would be available for consideration. Among them might be mentioned the suddenness of the price change, its relation to previous prices charged by the merchant or by others in the field in the particular locality or elsewhere, the existence or non-existence of new economic factors relating to cost of production, demand for the article, seasonal or other, the consequent need for expansion or contraction of the field for the particular merchandise and other factors, financial or economic, which might or might not warrant a precipitate reduction in price.

It has not been resolved whether 'unreasonably low' means that prices should be below full or direct cost. The questions of the unreasonableness of prices and predatory intent have been combined to give a single test - were the prices set at the low level for a predatory purpose or not? The Tenth Circuit noted that 524:

In the final analysis, the question resolves itself into one of intent and purpose, not a choice of accounting methods.

The ambiguity of the term 'unreasonably low' has caused some to question the constitutionality of the Section. If those wishing to obey the statute cannot fathom the meaning of a term in a criminal statute then it violates the dictates of due process and adequate notice. The Supreme Court ruled on this point in United States v National Dairy


524 Ben Hur Coal Co. v. Wells, 4 F.2d 481, 486 (10th Cir. 1957).
Products Corp.\textsuperscript{525} after a District Court had ruled that the statutory provision was "so vague, indefinite, and uncertain so as to violate the Fifth and Sixth Amendments to the Constitution of the United States"\textsuperscript{526}. The Supreme Court upheld the constitutionality of S. 3, finding that defendants were adequately forewarned of the illegal conduct. However, this decision was limited to "below cost" sales made "without legitimate commercial objective and with specific intent to destroy competition"\textsuperscript{527}.

(4) Conclusion

Despite the affirmation of the constitutionality of the Section, enforcement of section 3 is limited. It is accepted that it is not one of the antitrust statutes of the United States\textsuperscript{528}. Therefore the F.T.C. is precluded from enforcing the section, leaving the task to the Dept. of Justice which has shown reluctance to enforce any price discrimination legislation, let alone the criminal provisions of the Act. Private plaintiffs are also precluded from engaging in treble damages suits because the section is not an antitrust statute. Finally the difficulty of establishing knowledge or predatory intent, especially when higher criminal standards are required, has discouraged prosecution under the Section.

However, limited enforcement of S. 3 should not diminish the effectiveness of prohibitions against price discrimination and predatory

\begin{itemize}
  \item\textsuperscript{526} United States v. Bowman Dairy Co., 89 F.Supp. 112, 114 (N.D. Ill. 1949).
  \item\textsuperscript{528} Nashville Milk Co. v. Carnation Co., 355 U.S. 373, \textit{rehearing denied} 355 U.S. 967 (1958).
\end{itemize}
pricing. These practices are already covered by S. 2 of the Clayton Act, S. 5 of the Federal Trade Commission Act, and S. 2 of the Sherman Act. For this reason, S. 3 of the Clayton Act is seen by many as a superfluous addition to the U.S. statute books.\footnote{529}{Attorney General's Report, p. 201; Rowe, \textit{op. cit.}, p. 470.}
CHAPTER IV

EVALUATION OF THE ROBINSON-PATMAN ACT

4.1 INTRODUCTION

The Robinson-Patman Act cannot be seen as an antitrust statute. An evaluation of the Act reveals that it is a piece of protectionist legislation more akin to a price fixing statute than a statute to promote goals of competition and efficiency. It protects certain business groups from the rigours of competition, it leads to price rigidity and it leads to higher prices.

These detrimental effects may be seen from a survey of the Act. The jurisdiction of the Act is narrow allowing firms to circumvent the Act in ways that lead to price rigidity and inefficiency. The threshold tests for injury are low and the defences are hard to prove which, when coupled with the substantial cost of litigation, encourages the seller to adopt a path of per se legality rather than risk prosecution. The defences are inflexible and do not fill their objective of promoting efficiency and price flexibility. The cost justification defence encourages cost-plus pricing, while the meeting competition defence leads to inter-seller collusion.

4.2 THE JURISDICTIONAL ELEMENTS

The jurisdictional elements hold a special importance in the structure of the Robinson-Patman Act. They define the scope of the Act, the type of transactions that are per se legal and type of transactions to which prohibitions may be applied.

The jurisdictional elements of the Robinson-Patman Act have been
criticised for being too easy to prove and for being too narrow. The effect of this deficiency is to encourage firms to circumvent the Act in ways that decrease efficiency and harm competition. To be determined is whether it is desirable to rectify this fault by extending the jurisdiction of the Act.

(1) The Limitations on the Scope of the Robinson-Patman Act

The Robinson-Patman Act is orientated to dealing with the problems which Congress believed arose from the innovation of mass-merchandising in the 1930's. This explains some of the jurisdictional limitations of the Act. The Act covers the sale of goods but not services or intangibles. Agency and consignment arrangements, leases, credit arrangements and other forms of non-sale transactions are exempted. The 'sale' requirement removes non-consummated transactions such as offers to deal and executory contracts from the scope of the Act.

Limitations have also arisen because of express or implied restrictions on the regulatory powers of Congress. Congress may only legislate on inter-state transactions and intra-state transactions are exempted. The right of the trader to choose his customers is also sanctified and a refusal to deal is generally legal except where it is employed to further another illegal objective.

Other limitations have arisen simply because of the need to develop a workable statute. A simplified view of 'discrimination' is used. Devoid of any concept of 'business buccaneering' and unrelated to the economic definition of price discrimination, the term means simply a 'difference' in price. The 'like grade and quality' test is employed to limit the application of the Act to reasonably similar transactions and

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ensure that the Act does not require uniform profit margins on every commodity sold. And treating a subsidiary as neither a puppet nor independent of the seller is consonant with economic reality despite the inconsistency implicit in this approach.

(2) **Effects of the Limitations on Efficiency, Competition and Small Business.**

(a) **Per Se Legal Pricing and Distribution Systems.** The narrow ambit of the Act has allowed many firms to evade the provisions by adopting a *per se* legal distribution or pricing system. A firm wishing to avoid the provisions of the Act may:

(i) refuse to deal through some channels of distribution, preferring to deal with only one type or class of buyer (even though a refusal to deal should be seen logically as an extreme form of discriminatory dealing)**.

(ii) distribute through agency agreements, leasing arrangements, or other non-sale forms of distribution**.

(iii) make sales through subsidiaries who then redistribute the goods**.

(iv) supply goods of 'unlike grade or quality' to different buyers, either through product or brand differentiation**.

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2 For example, following a successful suit by the F.T.C. claiming Simplicity had granted discriminatory services and facilities to large buyers, (F.T.C. v. Simplicity Patterns Co., 360 U.S. 55 (1959)), Simplicity terminated its agreements with the disadvantaged buyers. This policy of refusing to supply those buyers was intended solely to coerce them to deter their private suits. See also Bird & Son, Inc., 25 F.T.C. 548, 553 (1937), and Comments, 58 Yale L.J. 1121 (1949).

3 Kintner, op. cit., pp. 41-42.

4 ABA Report, pp. 48-50.

5 Dept. of Justice Report, pp. 75-79. Although brand differentiated products are caught under the 'like grade and quality' test, buyers have recognised that they may receive discounts equal to the value of the consumer preference for the brand. Many large buyers (footnote cont. p. 223).
(v) employ a middleman to transport goods across a state line.\(^6\)
(vi) adopt a uniform-pricing system.\(^7\)

These alternatives available to the seller lead to inefficient distribution and inhibit the competitive process.

(b) Creating Inefficiencies. Because a seller adopts a distribution or pricing system which he would not have otherwise adopted but for the Act, the Act creates inefficiencies in distribution. Examples of such inefficiencies are the use of non-sale distribution systems, denial of supplies to otherwise efficient channels of distribution, and unnecessary vertical integration.

The unnecessary and wasteful proliferation of product and brand differentiation has caused special concern. Product differentiation increases production, inventory and distribution costs and decreases economies of scale. These costs are passed on to the buyers of both types of good. (The Dept. of Justice Report also suggests that more educated consumers are advantaged as they tend to recognize the artificiality of brand names and hence they save by buying private brand goods.\(^8\)).

Another source of inefficiency is the one-price system. The seller no longer prices in response to market forces. He may not even

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(footnote cont. from p. 222) have opted to distribute cheaper private-brand goods rather than the higher priced branded goods. Unbranded goods are, in theory, available to all buyers, however, in practice, they are available only to the large buyer with the volume necessary to sustain a private brand. Dept. of Justice Report, p. 76.

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\(^6\) Rowe, Price Discrimination Under the Robinson-Patman Act, p. 81.

\(^7\) Eg. see the alternatives suggested to Standard Oil by the Seventh Circuit, supra, p.114. See also the pertinent comments made in Klein v. Lionel, supra, p.73 n. 94 (continued on p. 74).

\(^8\) According to the testimony of Donald I. Baker, DCRG Hearings, Tr. 288-289, reported in the Dept. of Justice Report, p. 77.
recognise functions performed by the buyer, cost-savings resulting from the methods or quantities in which as buyer purchases goods, or any other discount system which requires differential pricing. The economic price discrimination that occurs distorts market mechanisms at the secondary and lower levels causing an inefficient allocation of resources.

(c) **Inimical Effects of Competition.** By evading the Act, the seller also reduces competition. The one-price system represents a non-competitive pricing system which is insensitive to the demands of individual customers of the seller.

The Act stifles competition between distribution systems as sellers are forced to ignore the most profitable system of distribution and instead favour the system which offers greatest security. Non-sale forms are advantaged over direct sale arrangements. Channels of distribution, which would once have increased competition in the market, are blocked as sellers distribute through one class of buyer.

(d) **Effects on Small Business.** Ironically, it is usually the small business that suffers because of these attempts to avoid the Act. The seller attempts to secure the patronage of the large buyer and, in so doing, harms the small buyers.

Consider the competition that exists between the large direct-buying retailer, and the wholesaler and small indirect-buying retailer. The seller may adopt a one-price system which may favour the direct-buying retailer more than would otherwise have occurred. Or alternatively the seller may refuse to supply the wholesaler, consequently harming both the wholesaler and the indirect-buying retailer.

The limited scope of the Act also means that the large buyer is not denied larger discounts although this was the primary objective of the Robinson-Patman Act. As well as taking the entire stock of the
seller, integrating vertically to secure higher functional discounts or buying the differentiated product from the seller, (usually a small buyer does not have the capacity to support a brand or product differentiated commodity), the buyer may buy on long-term contract or import the goods. Thus the Act cannot prevent the payment of excessive discounts to large buyers.

(3) Revising the Jurisdictional Elements.

A solution to these problems may be to extend the jurisdiction of the Robinson-Patman Act. The White House Committee on Antitrust Policy, (the Neal Committee) was particularly critical of the "irrational limitations" on the jurisdiction of the Act and proposed substantial reform:

a) That it shall be unlawful for any person in the course of commerce to discriminate, either directly or indirectly, in the exaction of consideration for the sale, lease, transfer or provision of any commodity or service where (i) the two or more transactions involved in the discrimination involve commodities or services of like grade and quality, (ii) such commodities or services are sold, leased, transferred or provided for use, consumption, or resale within the United States or any place under the jurisdiction of the United States, and (iii) the effect of the discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce.

(f) Nothing herein contained shall prevent any person from refusing to deal with any other person. Provided, however, that the offer to deal on discriminatory terms shall be treated as a completed transaction for the purpose of according relief under this section.

Many parts of the Robinson-Patman Act would be retained. The concept of discrimination, the 'like grade and quality' test and the right of a trader to choose his customers are all carried over from the Robinson-Patman Act. Although these may cause conflict with antitrust goals, they are seen either as administratively necessary or fundamental

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to the rights of individuals.

The major areas of reform are the inclusion of agency, consignment arrangements, leases and other forms of non-sale arrangements, services as well as commodities, offers to sell and executory contracts.

However, it has not been accepted that these or other reforms such as employing a wider 'like grade and quality' test, extending the Act to intra-enterprise transfers or extending the Act to intra-state transactions are necessarily desirable. This is for three reasons. Even though such reforms are intended to prevent firms circumventing the Act by bringing in a greater number and variety of transactions within its ambit, it is not clear that this wider jurisdiction will actually catch more undesirable discriminations. Second, the practical application of these reforms is questioned. And third, the Act has already had many undesirable effects on competition and efficiency (other than those mentioned here) and extending the Act may further aggravate this deleterious effects.

Extending jurisdiction to transactions involving services and to intra-state transactions may be counterproductive. Services tend to be provided by smaller firms. Intra-state transactions also tend to involve smaller firms. An extension of jurisdiction to these areas is more likely to disproportionately increase the regulatory burden of the small firms without providing compensating benefits in the form of increased control of larger firms. The ABA Report also provides an argument against the application of the law to intra-company transactions:

...application of the Robinson-Patman Act to intra-enterprise transfers could make artificial, stilted and cumbersome "transactions" out of what are otherwise simple transfers between related companies ultimately

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10 ABA Report, pp. 47 and 53.
11 ABA Report, p. 50.
sharing a single profit center. To require an equalization of "price" between owned and unrelated outlets could arguably jeopardize the efficiencies otherwise accruing from vertical integration in order to create the facade of arms-length transactions and superficial multiple profit centers.

Although the reforms remove the need to distinguish between sale/non-sale transactions, between goods and services and intangibles, and between consummated and unconsummated sales, the practical difficulties of implementing some of the reforms may outweigh their benefits. Distinguishing between an offer to sell and a mere invitation to treat and determining the terms of an unconsummated sale may prove difficult problems\(^\text{12}\). Applying the Act to offers to sell may also lead to more guarded price negotiation and further inhibit flexible pricing\(^\text{13}\). And while in sales transactions, prices are equal if the goods are homogeneous and methods of supply do not differ between customers (according to the philosophy of the Act which assumes a stable economy), non-sale arrangements incorporate many other factors such as risk of the agent or lessee, the responsibilities of the agent/lessee, etc., in their terms. Integrating provisions designed to deal with non-homogeneous customers may prove difficult, if not impossible, because of the many intangible factors involved. Finally, while application of the Act to services may seem logical, it also poses immense difficulties. The ABA Report summarises these difficulties\(^\text{14}\):

First, services and intangibles, more often than tangible commodities or mass-produced products, bear the imprint of the individuals performing or offering them and accordingly differ. Second, services and intangibles often are unique in the sense that identically defined output may involve differing circumstances and therefore require differing amounts of work. Third, since services frequently consist of a mix of tangibles and intangibles, the nature and extent of the service rendered may vary in

\(^{12}\) ABA Report, pp. 50-51.

\(^{13}\) Id.

\(^{14}\) ABA Report, p. 53, (footnote omitted).
accordance with the tangible commodity supplied. Finally, since services are frequently local in nature and regulated by state law, an expansion of the Act without redefining the "commerce" requirement might not bring a significant volume of service transactions under its coverage.

Thus the localised nature of services, the immense difficulties that would result from the 'like grade and quality' test, and the problems that occur when homogeneous output requires differing input seem to preclude application of the Act to services.

Extending the 'like grade and quality' test to cover a wider range of transactions and to eliminate product and brand differentiation may have the effect of bringing unlike transactions under the auspices of the Act. Already the test is criticised for ignoring consumer preference for branded products\(^{15}\). If the test were further expanded, many important commercial factors such as consumer preference and costs incurred would be relegated to the competitive injury and cost-justification provisions which have proven inadequate to deal with these considerations.

Finally, extending the jurisdiction may be undesirable because it brings further transactions within the ambit of an Act which has already proven unable to identify economic discrimination, and which fosters inefficiency and price rigidity. Rather than extending the jurisdiction, most commentators would prefer to see the problems remedied by the repeal of the Act.

(5) **Conclusion.**

There are pro's and con's in the argument for extending the jurisdictional scope of the Act. On the positive side, it would ease

\(^{15}\) See Rowe, op. cit., pp. 74-75; Cassady and Grether, The Proper Interpretation of 'Like Grade and Quality' Within the Meaning of Section 2(a) of the Robinson-Patman Act, 30 South. Cal. L.R. 241 (1957).
the task of enforcement because it removes the need to deal with
limitations such as whether newspaper advertisements are 'goods' or
'intangibles'. It removes the inconsistencies of the Act and prevents
easy circumvention of its provisions. On the negative side, it
increases the number and variety of transactions subject to the Act.
This may not be desirable if the Act is then applied to small
businesses, pro-competitive price discriminations or transactions that
are not sufficiently comparable to warrant equal treatment.

When weighing these arguments, the real question becomes whether
the Robinson-Patman Act can be tailored in such a way that it inhibits
anti-competitive price discrimination while promoting pro-competitive
price discrimination. As the jurisdiction becomes wider the Act must
become more discerning in its prohibitions. The focus is therefore on
the competitive injury test.

4.3 THE COMPETITIVE INJURY TEST

(1) Introduction.

The competitive injury clause is the most crucial part of the
Robinson-Patman Act. The competitive injury tests must be finely
balanced to catch those discriminations which impair competition, yet
leave unscathed the businessman's ability to fix prices to meet
market conditions.

Almost all commentators have criticised the competitive injury
tests applied at both the primary and secondary levels as being too
low. This has made it too easy to establish a violation of the Act.

16 Eg, see Dept. of Justice Report, pp. 10-17; Neal Report, C-8
- C-13; Rowe, The Federal Trade Commission's Administration of the
418-422; Elman, The Robinson-Patman Act and Antitrust Policy: A Time for
Reappraisal, 42 Washington Law Review 1 (1966), pp. 9-14; for a small
collection of these criticisms.
The result is that most discriminations within the jurisdiction of the Act are illegal whether they are anti-competitive and employed by a large firm or pro-competitive and employed by a small firm. A seller is dissuaded from adopting any type of differential pricing and instead encouraged to follow a course of per se legality.

In response, the Dept. of Justice and the Neal Committee have drafted alternative statutes governing price discrimination. Their proposals apparently represent a radically new way of approaching the competitive injury problem. However, these are fairly close to the tests which are currently being used by the Courts. The Neal Report refers to competitive injury in subsection (a) and this reference is modified in subsection (b):

b) A discrimination shall be held to have the effect described in subsection (a) only where:

(i) The recipient of the benefit of the discrimination is in competition with others not granted the same treatment, the discrimination is substantial in amount, and the discrimination is part of a pattern which systematically favors larger competitors over their smaller rivals; or

(ii) The recipient of the benefit of the discrimination is in competition with others not granted the same treatment, the discrimination is substantial in amount, and the discrimination imminently threatens to eliminate from a line of commerce one or more competitors whose survival is significant to the maintenance of competition in that line of commerce; or

(iii) The person granting the discrimination is in competition with others serving significantly more limited areas (territories or classes of customers which are relevant lines of commerce), the discrimination is restricted to one or more such limited areas (representing a small part of the total area served by the person granting the discrimination), the consideration exacted in such limited areas is less than the reasonably anticipated long-run average cost of serving those areas (including capital costs), and the discrimination imminently threatens to eliminate from such a limited area one or more competitors whose survival is significant to the maintenance of competition in that area.

Provided, however, that the survival of a competitor is not significant to the maintenance of competition where, in the line of commerce affected, the number of competitors remaining, or the ease with which new
competitors may enter, indicates that effective competition will not be suppressed for an appreciable period of time.

(2) Secondary Line Injury

The first two sections of this revision refer to secondary line discrimination. They contain several important features -

(a) They codify the Morton Salt inference that a systematic discrimination will cause injury to competition.

(b) They apply only where the favoured buyer is large.

(c) They apply only to secondary line competition.

(a) The Inference of Injury Rule. Competitive injury at the secondary level occurs from the granting of discounts over a long period of time. Shifts in market shares are almost impossible to detect and so actual injury is hard to gauge. Therefore it has been necessary to apply general rules which allow an inference of injury. The Morton Salt test was developed to deal with cases where actual injury was negligible. The Neal Committee (and also the Dept. of Justice) codify this general rule that substantial discriminations granted on a systematic basis distort competition at the secondary level.

The Dept. of Justice Report summarizes the assumptions on which the Morton Salt inference is based:

(i) if any price discrimination is permitted, the practice will become generalized,

(ii) 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 will be forced out of business, and

(iii) if similarly-situated disfavoured purchasers were forced out of business, then the structural change would be severe enough to

17 Dept of Justice Report, p. 225.
affect the competitive vigour of the remaining firms in the market.

The Report argues that these assumptions are essential to the workings of the Act. This is shown by the Morton Salt case. However, these assumptions lower the threshold test for injury and therefore lead to the prohibition of both pro- and anti-competitive price discrimination.

(b) Focus on the Big Buyer. Another salient feature of the revision is that it focuses only on the big buyer. This resulted from criticism of the enforcement of the Robinson-Patman Act - many claiming that the F.T.C. focussed on the smaller buyer rather than the large buyer who, because of his buying power, could cause injury to competition. The large buyer is precluded from obtaining relief when a smaller buyer receives a discrimination, even when that discrimination is granted on a systematic basis.

(c) Tertiary Line Injury and Beyond. The competitive injury clause is confined to discriminations that cause injury to secondary line competition. Competition at the tertiary line and beyond is excluded. Arguments against the extension of price discrimination law to tertiary line injury are based mainly on the Standard Oil Co. case. That factual situation lead to F.T.C. to grant an Order (affirmed by the

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18 Dept. of Justice Report, pp. 221-228.

19 Former F.T.C. Chief Economist Corwin Edwards states "[m]any proceedings under the Robinson-Patman Act have involved neither predatory discrimination by sellers nor buying advantages for powerful purchasers. In each field of activity some of the cases have been irrelevant to the purposes of the law". The Price Discrimination Law, p. 627.

20 See the objection of Commissioner Nye to the Act's focus on large buyers. Hearings before the Ad Hoc Subcomm. on Antitrust, the Robinson-Patman Act, and Related Matters of the House Comm. on Small Business, 94th Cong., 2d Sess. 102 (1976).

Court of Appeals), that seemed to require the manufacturer to police the resale prices of the distributor. This would be contrary to the per se ban on Resale Price Maintenance imposed by the Sherman Act. It was this conflict with the Sherman Act that lead to the omission of tertiary line competition. It seems that an Order compelling Resale Price Maintenance may be necessary if tertiary line competition is to be protected. If a manufacturer grants a discount to a buyer and he cannot justify it by other means such as cost justification or meeting competition, the only way he can ensure that it is not passed on to tertiary buyers is to:

(i) make the discount so small that it cannot be passed on to the tertiary level, (which defeats the purpose of the discount), or

(ii) match the prices at which he and the distributor sell to retailers. This demands some form of Resale Price Maintenance or collusion between the seller and the buyer. In such a case, there is direct conflict between the Robinson-Patman Act and antitrust principles.

There are other reasons for not applying the competition test to levels below the buyer's level -

(i) Cases of tertiary line injury are likely to be rare, both because the discount is likely to have been dissipated or diluted by the time it reaches the level of the buyer's customer, and because the distribution structure amenable to tertiary line injury is less common. Therefore to enforce a law against such injury is likely to place an unnecessary burden on F.T.C. resources.

(ii) Some discounts passed on by a buyer to his competitors may be desirable. In the situation where the seller grants a functional discount to encourage the buyer to perform certain distribution

22 Neal Report, C-8
functions that the seller would otherwise have performed, if the buyer performs these functions more efficiently than the seller, then he will pass on the functional discount to the buyer without causing economic inefficiency.

(iii) It is difficult to discern whether the discount passed on to the buyer's customer originates from the discount granted by the original seller or whether it results from the independent pricing practices of the middleman.

(iv) If such a policy were enforced, a seller may be encouraged to sell to only one class of customer rather than face prosecution for causing tertiary line injury.

(3) **Primary Line Injury**

The primary line injury tests used in early F.T.C. cases have been heavily criticised for inhibiting pro-competitive price discrimination. Again, this anti-competitive result has occurred because a low threshold of injury to a particular competitor has been sufficient to establish a violation. The major case on determining primary line injury, *Utah Pie*, is an example where price cutting by national sellers was prohibited even though it served to undermine the monopoly position of a local competitor. The Supreme Court indicated that selling below full cost, aggressive statements about competitors or diversion of trade from a competitor, could all be illegal when coupled with price discrimination.

Sensing the danger of such low threshold tests, some Courts have adopted standards similar to those used in Sherman Act cases. The primary line standards proposed in the Neal Report are an attempt to codify those doctrines. One of the purposes of the revision was to reverse the result given in the Supreme Court's *Utah Pie* decision.²³

²³ Neal Report, C-12.
The proposals raises the threshold test of injury by requiring that -

1) the seller be larger than his competitor,

2) the discrimination be confined to a small area served by the seller,

3) the consideration received by the seller be less than 'reasonably anticipated long-run average cost', and

4) the discrimination have the effect of eliminating one or more competitors whose survival is significant to the maintenance of competition.

While most agree that the standards employed by the Supreme Court in Utah Pie are undesirable, the Neal Report proposals also have many deficiencies. These proposals -

(a) link price discrimination and predation, and

(b) exclude predatory intent,

(c) in favour of a cost-based test for legality.

(a) Predation and Price Discrimination. The Neal Report continues to link price discrimination and predation despite strong arguments that price discrimination merely supports predation. Price discrimination and predation are linked by the subsidization theory. The high price in one market subsidizes the predatory low price in the other market. However Bowman points out that it is illogical to link price discrimination and predation. This link confuses the cause of the injury, the low price, with the method of financing that low price, the monopolistic high price. A predator could equally well finance his activity with monopoly profits gained from another product line, or even with money received from a legacy from a wealthy relation! Nor does the seller wait until he grants a predatory price before he sets his

24 Bowman, Restraint of Trade by the Supreme Court: The Utah Pie Case, 77 Yale L.J. 70 (1967).
monopolistic price in the second market. There need be no relationship at all between the actions of a discriminator in the two markets that he operates, and the presence of price discrimination and inter area subsidization are of lesser concern than the predatory low price or the monopolistic high price.

However, this link might be justified for two reasons. Although price discrimination and predation need not be linked in theory, in practice predation will almost always occur in conjunction with discriminatory pricing, especially when one firm serves more markets than the other as is required by the proposals. Second, the Neal Committee proposals do not require that the injury be the effect of the discrimination, as does the Robinson-Patman Act, (although the Courts seem to have written this requirement out of the Act).

The arguments against such a link are that it is theoretically unsound and unnecessarily raises the jurisdictional elements necessary to establish a violation. The Dept. of Justice recognized that price discrimination and predation need not, nor should not, be linked. Their proposals illustrate how a statute against predation might be formulated.

S. 2. It shall be unlawful for a 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 of whether any overt action is taken to fulfill such threat.

S. 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.

The proposal allows a 'meeting competition' defence, a 'changing market conditions' defence and a 'no competitive injury' defence, all applicable to Section 3 only. A further defence to Section 3 is if the seller is a new entrant - a new entrant defined as a person having at the time of sale 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. This defence allows promotional pricing and reiterates the concern with large and not small sellers.

In addition many of the terms of the Act are defined:

S. 5...(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.

(60 days is meant to approximate the economist's concept of 'short-run').

Although conceptually superior to the Neal Report proposals because they focus on the cause of the injury - the low price, these proposals are not without criticism. The most controversial aspects are the use of the Areeda and Turner Marginal Cost test and the absence of a
(b) Predatory Intent. Both the Justice Dept. and Neal Report revisions omit a test of predatory intent. The reason is that predatory intent can rarely be distinguished from pro-competitive behaviour. The Neal Report states:

No reference is made to "predatory intent", and none of the standards specified calls for a finding on the issue of "predatory intent". Interpretations of intent are particularly perilous in this area and, as illustrated by the Utah Pie case, the concept may be manipulated to support improper results.

Many authors agree that attempting to discover the seller's intent is difficult and treacherous:

The predatory nature of temporary price cutting, where it is present, is a reflection of the aggressor's intention, which is to eliminate its rival as an independent competitor, not through the exercise of greater efficiency in the usual sense but through a pricing manoeuvre containing an undertone of threat. Such intention is obviously difficult to establish conclusively, and can be inferred with reasonable confidence only when the observer, be he judge or academic, has been able to gain a detailed and thorough understanding of the surrounding circumstances in all their complexity.

The alternative is to base a test of unlawfulness on the costs of the seller. However, the difficulties of this approach must also be recognized:

Any attempt to narrow the definition [of predation] by inserting in it the requirement that a reduced price be lower than cost (in some sense) would be inappropriate, since it has been shown...that selling at reduced prices above cost can serve the same purpose in the context of predatory intent.

(c) The 'Below Cost' Standard. Although a 'below cost' standard may be an inaccurate surrogate for 'intent', it does have the advantage


of being a more objective standard.

Several 'below cost' tests are available, although the test that has received greatest acceptance by the Courts is the Areeda and Turner marginal cost test. Areeda and Turner derive their test from economic analysis. They argue that long-run marginal cost is the relevant criterion for distinguishing between pro- and anti-competitive pricing.

A seller may price at below marginal cost, between marginal cost and full cost, or above full cost. However, a seller would be acting irrationally if he were to sell at below marginal cost:

[M]arginal-cost pricing leads to a proper resourse allocation and is consistent with competition on the merits. Neither reason obtains when the monopolist prices below marginal cost. The monopolist is not only incurring private losses but wasting social resources when marginal cost exceed the value of what is produced. And pricing below marginal cost greatly increases the possibility that rivalry will be extinguished or prevented for reasons unrelated to the efficiency of the monopolist. Accordingly, a monopolist pricing below marginal cost should be presumed to have engaged in a predatory or exclusionary practice.

Any price at or above marginal cost would be per se legal. If he sells at marginal cost then the only competitors who would be unable to make a profit would be those who are less efficient than the seller.

A seller has a number of profit-maximising reasons why he might wish to price at between marginal cost and full cost. These reasons may include clearing stock, promotional pricing, etc. Even if a price above marginal cost is employed for a predatory purpose (eg. limit pricing or drastic temporary price cuts) and is not profit-maximising in the short term, Areeda and Turner would allow this pricing to continue. Only


30 ibid, at p. 712.

31 Limit pricing is pricing at above marginal cost but still at a low level for an extended period of time such that the predator continues to cover costs while his competitors leave the market.
less efficient firms will suffer larger losses per unit of output; more efficient firms will suffer smaller losses or even operate profitably.

Although the predator may have sufficient resources to destroy an equally efficient or more efficient rival and this might have inefficient and anti-competitive consequences, the alternative of setting a price above marginal cost is more unattractive because it restrains aggressive pricing and therefore allows less efficient firms to survive against their more efficient opponents. The marginal cost rule also achieves a social optimum because any other rule based on a higher cost-standard would force prices to a higher level and reduce output.

To ease implementation of their rule, Areeda and Turner substitute 'average variable cost' for marginal cost. There would be no prohibition if there are significant diseconomies of scale and marginal cost exceeds average variable costs. They would also introduce more flexibility into their rule by allowing 'reasonably anticipated' average variable costs. Areeda and Turner would not allow any exceptions to their rule. Thus a defence of promotional pricing or meeting competition would not be accepted.

(d) Conclusions. The Areeda and Turner test provides a clear standard for predatory conduct, and makes redundant the tests used in Utah Pie, such as below-full cost pricing, inference of intent from aggressive statements from rivals and diversion of trade. As noted earlier, the Areeda and Turner test has gained favour with some Appeal Courts, notably the Fifth, Seventh, Ninth, and Tenth, although their rule has been modified in some cases to include a finding of predatory intent where the monopolist prices between marginal cost and average total cost.\(^{32}\)

\(^{32}\) See supra, pp. 88-89.
The marginal cost rule has not gone uncriticized. Even Areeda and Turner recognise that the test does not prevent all cases of undesirable pricing. Limit pricing may in the long-run eliminate competitors. A related problem is that the test is too specific and would remove some of the flexibility which such vague concepts as 'predatory intent' give to the Sherman and Robinson-Patman Acts.

However, the introduction of precise rules for determining legality of pricing and the rejection of the vague standards of predatory intent that have prevailed would be welcome changes to the law. Certainly the major contribution of the Areeda and Turner test is that it increases the threshold test for primary line injury and thereby exempts more discriminatory pricing. This in turn leads to greater pricing flexibility.

By raising the threshold standards of injury, the test rejects the 'incipiency' rationale that lead to the introduction of the Robinson-Patman Act and equates the primary line standards used in Sherman Act and Robinson-Patman Act cases. (Indeed, the test was formulated for Sherman Act cases). This suggests that the price discrimination provisions are superfluous and cases of predation should be considered under the Sherman Act.

4.4 DEFENCES PROVIDED BY THE ACT

(1) Meeting Competition

(a) The Flexibility of the Defence. Many of the controversial areas of the meeting competition defence have already been solved satisfactorily by the Courts as they attempt to develop a workable defence. It has been accepted that a seller may adopt a pricing system or lower prices over a geographic area where he has reason to believe the competitor's price is available to all or most buyers in that area. A seller may inadvertently beat a competitor's price. And the Callaway Mills case indicates that a seller might be able to meet competition irrespective of the legality of the competitor's price. This flexibility has arisen mainly as a result of the 'good faith' doctrine which is central to the defence.

The last major area to be clarified is whether the seller may adopt an illegal industry-wide pricing system and claim that he was merely meeting competition. By allowing the reciprocity argument, the Commission surrenders the power to pursue pricing systems which facilitate tacit or express collusion.

(b) The 'Lying Buyer'. These have not been the only problems with the defence. There has been direct conflict between the Sherman Act and Robinson-Patman Act because of the implication that inter-seller price verification may be allowed by the meeting competition defence. Although recently the Supreme Court indicated that inter-seller verification was not necessary and nor would inter-seller verification be tolerated under the Sherman Act, they did not answer how a seller could verify a competitor's price. It seems that a 'good faith' effort may be satisfied by showing that a buyer threatened to close his account or that other buyers also received similar offers. However, the former option provides scope for the 'lying buyer'. A fine line must be drawn to ensure that
the lying buyer does not extract undue concessions, yet ensure that price verification does not violate the Sherman Act.

(c) Fundamental Conflict with Antitrust Principles. The very concept of 'meeting competition' provides a fundamental conflict with antitrust principles. The meeting competition defence encourages price uniformity between competitors because it allows all firms to meet but not beat the lowest prevailing price in a market. In this way, the defence sets a floor on prices and this floor also becomes the ceiling as firms match this minimum price. The reciprocity argument is only one obvious area where the defence encourages uniform pricing within an industry and leads to tacit or express collusion, yet the problem as it relates to pricing systems is only a small part of the total problem of price uniformity. The defence is inherently anti-competitive and there is no solution to this problem if the law is to allow a seller to take defensive action to protect himself against other sellers.

(2) Cost Justification

(a) The Failure of the Cost Justification Defence. The cost justification defence represents one of the major areas where the Act has failed to achieve its objectives. The defence was introduced to allow a seller to pass on any efficiencies that may arise from the methods or quantities in which the buyer purchases the goods. Because it has failed in that objective, the Act has discouraged the development of more efficient forms of distribution and protected unnecessary middlemen from competitive forces.

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34 For a critical analysis, see Dept. of Justice Report, p. 18; Attorney General's Report, p. 169. However, see Copeland, Significance of the Cost Defense, [11 Antitrust Bull. 925 (1966)], who, after conducting an extensive evaluation of the incidence of the defence, including cases where no formal action was taken by the F.T.C., concludes the defence has real significance in the informal settlement proceedings. This supports the view of Taggart who claims the defence "is the most practical and available", Cost Justification, p. 549.
The cost-justification defence has failed for many reasons. The accounting definition of cost is too narrow and does not extend to economic costs, even though recognition of such costs is essential if the defence is to adequately reunite the legal and economic concept of price discrimination. A pertinent example of this inadequacy is the failure to recognise the opportunity cost of capital as a relevant cost.

The defence requires cost-savings to be justified by reference to full costs, however, this usually demands that the seller allocate indirect costs to different purchasers or products. Any allocation is, by its very nature, essentially arbitrary. Therefore an attempt to cost-justify a discount system will be fraught with uncertainty. While classification systems and statistical techniques may help the seller, the rigid and conflicting interpretations by the F.T.C. have created confusion about the appropriate way to allocate costs. This failure of the defence is unavoidable because of the need to use full costs and not incremental costs.

Cost justification is expensive and time consuming. Much of the information required is not readily available from accounting records and it is necessary to develop comprehensive studies to satisfy the high standards required by the F.T.C.

Some of the fault for the failure of the defence rests with the rigid and inflexible interpretations given by the F.T.C. Conflicting judgements and high standards of proof have deterred many sellers from attempting the defence. There are no clear guidelines to assist the business person to construct a cost justification defence. Indeed, the Supreme Court noted that "cost justification being what it is, too often

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no one can ascertain whether a price is cost justified.\textsuperscript{36}

The defence also concentrates on actual costs on the assumption that those costs are known to the seller prior to making the pricing decision. This is not usually true, yet accepting this assumption requires that a seller begin a comprehensive cost study prior to granting discriminatory terms. Thus it is not just those firms actually facing prosecution that must initiate a cost study but all firms who grant discriminatory prices.

A related problem is that the 'due allowance' term has not been interpreted in a flexible way. Sellers are unduly penalized for errors in pricing even though the 'due allowance' principle was intended to add flexibility to the defence.

(b) Inefficiencies Resulting from the Failure of the Defence. The effect of the failure of the cost-justification defence is to prevent sellers passing on -

(i) cost savings that result from the more efficient methods or quantities of purchasing\textsuperscript{37},

(ii) cost savings reimbursing the buyer for functions performed on behalf of the seller.

The Neal Committee has attempted to improve the defence. They suggest repeal of the Quantity Limits proviso. It serves no purpose other than to inhibit the recognition of cost savings resulting from the quantities in which a buyer purchases goods. They also suggest that the seller be allowed a greater margin of error when establishing the defence and that he be allowed to use either actual or anticipated costs. The classification system is sanctioned provided it is


reasonable and, if found unreasonable, the onus is placed on the enforcement agency to suggest an acceptable alternative:

(d) It shall be a defense to a charge of discrimination that the lesser extraction of consideration makes an appropriate allowance for differences in the cost of manufacture, distribution, sale or delivery resulting from the differing methods or quantities involved in the transactions in question. An allowance is appropriate where the difference in consideration does not substantially exceed the difference in cost; where the difference in consideration does not exceed a reasonable estimate of the difference in cost; or where the difference in consideration 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 consideration between classes approximate differences in cost. If a system of classification is held to be unlawful, the court or agency so ruling should indicate either (i) that the seller's customers are so similar in pertinent characteristics that no system of classification would be valid, or (ii) that a system of classification described by the court or agency may properly be employed in lieu of the one held to be unlawful.

However, this reform cannot relieve the difficulties created by an inflexible enforcement agency. Nor does it extend the concept of 'cost' to include opportunity costs.

Nor can the reform of the defence ever succeed. The Act contains an assumption concerning the relationship between prices and costs which is fallacious. The Act assumes that costs determine prices \(^{38}\). This is not true:

(i) The judicial/accounting concept of cost is more narrow than the economic concept of cost and therefore costs such as investment costs are excluded from the defence.

(ii) There is no proper way to allocate joint costs.

(iii) Most importantly, 'price' is based on factors other than cost. These other factors may be placed under the myriad heading of demand and supply conditions. Examples are the willingness of some

\(^{38}\) Liebeler, Let's Repeal It, 45 A.B.A. Antitrust L.J. 18 (1976), p. 41.
customers to pay more than other customers, or changes of supply conditions over time and between regions. In fact, because price affects sales volume and hence production volume, it is price that determines cost and not visa-versa.

Because the Robinson-Patman Act makes this invalid assumption about pricing, the Act directly interferes with the market pricing mechanism and thereby creates inefficiencies in the operation of the market. For this reason the Act should be seen as regulatory. There is no way to construct an Act which avoids making this totally incorrect assumption.

(3) Functional Discounts\(^{39}\).

One of the major ways in which the Act has inhibited the development of efficient distribution systems is by preventing a seller granting functional discounts to reimburse a buyer for functions rendered. A buyer who performs a function on behalf of the seller should not be prevented from assuming that function. Presumably he performs it because he can do it more efficiently then the seller and thus the seller, the buyer, and the consumer all benefit from the more efficient form of distribution that results.

The Act prevents buyers assuming functions normally performed by the seller by preventing sellers reimbursing buyers for those services. This has been occurred because of -

(i) the Indirect Purchaser doctrine,

(ii) the failure of the cost-justification defence, and the resultant necessity to justify functional discounts by showing lack of competitive injury,

(iii) the Brokerage clause.

(a) The Indirect Purchaser Doctrine. The use of a "dummy

\(^{39}\) See Dept. of Justice Report, pp. 84-88; ABA Report pp. 54-72.
middleman" to subvert the Act provides a serious problem. A seller may establish a dummy middleman, sell to this middleman and to the favoured buyer at equal prices and then resell the goods (via the middleman) to the disfavoured buyer at some higher price. By introducing the middleman, the seller sells at a uniform price, the two buyers buy at different prices and there is no come-back because they do not buy from the 'same seller' as is required under the Act.

To prevent this the 'Indirect Purchaser' doctrine has been applied to cases where the seller in some way controls the resale activities of the middleman. But this doctrine insists that two buyers receive the goods at the same price and ignores the possibility that the middleman, whether he be real or dummy, may provide genuine services for which he is entitled to charge the buyer. Purolator Products, Inc. is typical of this situation.

It is suggested that the doctrine be limited to cases where the middleman performs no genuine functions. Alternatively, the middleman should be allowed the same defences of lack of competitive injury and cost justification as the seller, allowing him to justify a legitimate functional discount. Until this change is made, the doctrine will continue to inhibit desirable functional discounts and thereby reduce efficiency.

(b) Restriction of the Cost Justification Defence and Resort to 'Lack of Competitive Injury'. Although functional discounts are conceptually based on cost savings of the seller, the failure of the cost justification defence has meant the seller must grant discounts only if he does not cause competitive injury. Alternatively he may use a one-price system and eliminate functional discounts altogether.

By relying on the 'lack of competitive injury' defence, the functional discount structure must conform with the distribution structure - ie. a distributor gets the greatest discount, a direct
buying retailer gets a lesser discount. This discount structure no longer necessarily accords discounts to those who perform the functions; only to those who are higher in the distribution channel. Some retailers have integrated backwards and perform the functions of a distributor. Direct buying retailers and co-operatives are two prominent examples. The 'lack of competitive injury' defence discourages backward integration by allowing discounts to buyers only if according to the level at which they resell the goods.

The victims of this anomaly are the chain-store, the co-operative and any other vertically integrated distributor-retailer. The penalisation of the co-operative is ironic considering it usually consists of small businesses banded together to allow them to compete more effectively with larger firms. The case of the dual distributor provides a glaring anomaly. He may receive functional discounts on goods that he resells at the wholesale level but is denied such discount on goods which he resells at retail. The strange consequence is to encourage different prices for identical goods brought at the same time from the same seller. This is clearly contrary to the (supposed) objective of the Act to eliminate economic price discrimination and promote efficiency.

The inhibition of functional discounts prevents inefficient manufacturer-wholesaler-retailer distribution systems being challenged by new vertically integrated systems. It has been noted that:

...by imposing a serious risk of law violation upon the charging of lower prices designed to induce and compensate the performance of additional functions, the Act tends to discourage experimentation with new systems of marketing which may eliminate or by-pass traditional avenues of distribution and thus may contribute to marketing efficiency and the overall enhancement of competition.

This failure results from the combination of the cost justification defence and the competitive injury defence. Possible solutions are:

(i) To accord function discounts according to the level at which the buyer buys rather than the level at which he sells. This recognises that the level at which a buyer buys usually indicates the highest functions which he performs.

(ii) The Act could allow sellers to reimburse buyers for additional costs incurred by the buyer. This is justified as the presence of countervailing costs negates the competitive advantage of a discriminatory discount and therefore there is no competitive injury\(^{41}\).

(c) The Brokerage Provisions. Brokerage is like any other function in the distribution process. However, the Robinson-Patman Act treats it in a fundamentally different way than other functions. A seller may not cost-justify brokerage discounts, nor may he show that there is a lack of competitive injury. The treatment of brokerage is radically out of line with other functions. To bring consistency to the Act, the brokerage provision should be repealed.

4.5 BUYER LIABILITY

The prohibition against granting discriminatory discounts has placed the seller in a dilemma of having to decide whether to adhere to the law and possibly lose a valuable customer or to violate the law and retain the customer. To support the seller, the buyer-liability clause was introduced giving liability to the buyer who knowingly induces a discriminatory discount.

The buyer-liability clause does not help the seller – he is

still faced with the dilemma of breaking the law or losing a customer. It merely extends liability to buyers.

The buyer liability clause introduces its own dilemma. The buyer may be faced with a Robinson-Patman offence even though he was pursuing the normal competitive activity of bargaining for discounts\textsuperscript{42}. Of course this is the intention of the section, but this dilemma is a prominent example of the way in which the Act replaces price flexibility with price rigidity. The Act discourages and penalizes normal free bargaining between the buyer and the seller and leaves oligopolistic industries shielded from the pressures of large buyers seeking to break up high prices.

To avoid tampering with the bargaining mechanisms which form the basis of our competitive system, the buyer-liability standards must be raised. The Neal Committee would retain the current buyer-liability clause, however, they note that a buyer violation requires a violation by the seller and higher standards of seller-liability will bring a concomitant rise in buyer-liability standards. It will also make it less likely that the buyer will have culpable knowledge of the seller's violation and this should further decrease the likelihood of finding a buyer violation\textsuperscript{43}.

4.6 THE PER SE PROVISIONS

(1) The Brokerage Provisions

The brokerage provisions have received heavy criticism\textsuperscript{44}. In

\textsuperscript{42} See Dept. of Justice Report, p. 32.

\textsuperscript{43} See the Neal Report, C-23 - C-25.

\textsuperscript{44} Justice Dept. Report, p. 80; Attorney General's Report, p. 187-193; David M. Goeder, The Robinson-Patman Act: Section 2(c), (d) and (e), from Conference on the Antitrust Laws and the Attorney General's Committee Report, reprinted in 11 Jnl. Reprints for Antitrust Law and Economics 616 (1980), Elman, op. cit, pp. 21-25.
particular,

(i) the provisions are not concerned with discriminatory brokerage discounts, (although the Supreme Court has still to have the final word on this issue),

(ii) it has not been recognised that the broker can benefit both the seller and the buyer. Therefore the complete prohibition on the passing of brokerage from one sales party to the other is misguided\(^{45}\),

(iii) the treatment of brokerage is inconsistent with other forms of price discrimination. There is no competitive injury section and the cost-justification and meeting competition defences are not allowed. One unfavourable effect of the lack of competitive injury clause is that the defendant has often been a small firm.

(iv) the provision has consumed vast amounts of F.T.C. resources\(^{46}\).

The effect of the brokerage provision has been to protect independent brokers, and prevent buyers performing their own brokerage function and receiving reimbursement for this function from the seller. This has particularly harmed co-operatives of small buyers who have seen brokerage as one of the important ways where they can make cost savings. The Attorney General's Report states\(^{47}\):

> 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.

Almost all commentators recommend repeal of this section and the treatment of brokerage as an ordinary function under the main price

\(^{45}\) Gooder, op. cit., p. 622.

\(^{46}\) Of 439 final orders issued from 1936-1969, 180 have been made under the brokerage section.

\(^{47}\) Attorney General's Report, p. 191.
(2) The Promotional Allowances and Services Provisions

The promotional allowances and services section has not received the same level of criticism as 2(c), possibly because the F.T.C. has been willing to give a flexible interpretation to the section. The problems that have arisen relate to:

(i) the offering and granting of promotional allowances and services to small firms, even though the firms are too small to use these promotions effectively. This has undesirable effects because the seller is forced to offer schemes even though there is little chance that many buyers will participate.

(ii) A seller might also forgo any schemes which benefit him only if limited to large purchasers.

(iii) the application of the per se rules represent inconsistent treatment of this form of price discrimination.

According to the Neal Committee, the solution to these problems is to treat promotional allowances and services as an ordinary form of discrimination thereby introducing a competitive injury test. However, even under the main price discrimination provisions the requirement of proportionate equality can still compel inefficient promotional allowances and services.

4.7 ENFORCEMENT OF THE ROBINSON-PATMAN ACT

(1) F.T.C. Enforcement Priorities

Although the Robinson-Patman Act does not address the major causes of business concentration such as price fixing, mergers,

48 Neal Committee; Dept. of Justice Report, pp. 267-269; Attorney General's Committee; Elman, Op. Cit., pp. 21-25.

49 See generally Dept. of Justice Report, p. 91.
monopolisation, excessive promotional expenditure, etc, enforcement of
the Act prior to 1970 consumed almost 50% of the F.T.C.'s limited
resources. This, in itself, would suggest that the Act has had an
anticompetitive effect by drawing F.T.C. resources away from more
important areas of antitrust.

Two reasons for this drain on resources have been identified.
First, price discrimination cases must be supported by evidence of
market structure, barriers to entry and conduct of market participants.
Providing this information requires substantial resources. Second, the
ease of receiving a favourable verdict has attracted resources as the
F.T.C. attempts to play the 'numbers game' - that is, obtain the highest
number of successful prosecutions. The fault here is the low
jurisdictional and competitive injury requirements of the Robinson-
Patman Act.

This penchance for the easy case can also be seen by an
examination of data on cases brought by the F.T.C. under the individual
sections.

Table 1. Enforcement by the F.T.C. by Section, 1936-1969

<table>
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<th>Section</th>
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It is readily seen that the F.T.C. has pursed cases brought under the \textit{per se} provisions even though these provisions cover only indirect discriminations. There has been a notable lack of enforcement of 2(f), partly as the aftermath of the \textit{Automatic Canteen} decision. Nevertheless this indicates the Act has failed to attack the main culprit, the powerful buyer\textsuperscript{52} and instead is directed at the seller.

Nor has the F.T.C. distinguished between large and small firms. Rowe notes\textsuperscript{53}:

On a purely quantitative scale, the F.T.C.'s Robinson-Patman enforcement has hit the pygmies notably harder than the titans of the trade. Out of the 1,040 formal complaints issued during the F.T.C.'s first twenty-five years of Robinson-Patman enforcement, only 28 per cent smote corporations noticed by a listing in \textit{Moody's Industrials} for 1960, and only 13 per cent charged concerns ranked among \textit{Fortune's} 1961 directory of the 500 largest industrial of the 50 largest merchandising corporations in the United States.

When the buyer-liability clause was re-activated in the late 1950's, the F.T.C. focussed on joint-buying groups set up by small automotive parts distributors to secure economies of pooled purchasing for their members in competition with large retail chains. Similarly, the brokerage provisions have been used heavily against small firms\textsuperscript{54}. Rowe summarizes the situation\textsuperscript{55}:

\begin{quote}
...the skewed statistical record portrays a Parkinson's Law of F.T.C. enforcement: Robinson-Patman proceedings proliferate with the ease of making a case.
\end{quote}

\textsuperscript{52} Of 37 F.T.C. complaints against large buyers from 1936-1963, 3% of all charges, only 11 cases involved buyers of national prominence, of which 8 cases were dismissed and 3 led to Orders. Rowe, The Federal Trade Commission's Administration of the Anti-Price Discrimination Law, p. 430.

\textsuperscript{53} \textit{Ibid}, p. 430.

\textsuperscript{54} Of 344 Brokerage complaints from 1936-1963, 10 involved firms of national stature, of which 4 were dismissed and 6 resulted in Orders. \textit{Ibid}, p. 431.

\textsuperscript{55} \textit{Ibid}, p. 432.
(2) The Breath of F.T.C. Orders

The breadth of F.T.C. orders has caused anti-competitive results and the "compliance" phase of Robinson-Patman enforcement has assumed huge dimensions as F.T.C. staff continue to monitor industries for violations of Orders.

Rather than evaluate every present and future pricing decision of a firm, the F.T.C. have often employed broad Orders which enjoin the respondent from any repetition of the offence and also prohibit any conceivable violation of the pertinent statutory provisions in any manner anywhere. In many cases, such Orders are obtained on a 'mass' basis from firms in an industry (presumably with significant savings in F.T.C. resources). One quickly realizes that these long-standing Orders serve to inhibit pricing flexibility in an industry and require substantial resources to monitor. When enforcing these Orders, the F.T.C. is placed in the position of either dedicating enormous resources to the task, or allowing many possible violations and encouraging firms to engage on a course of "legal brinkmanship".

In response to this the Neal Report would place a limit on F.T.C. Orders:

(i) Any order issued to enforce this section 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 the order remain in effect more than five years after its date of issue.

(3) Private Enforcement

The fear of private enforcement serves to discourage any

56 Dept. of Justice Report, p. 33.
57 Neal Report, C-26.
58 See generally Banta & Field, op. cit.
potential violation of the Act\textsuperscript{60}. The cost to the defendant of a private suit includes treble damages, the legal costs for himself and the plaintiff, private costs of litigation such as the cost of attempting defences and the social consequences of a violation. The fear of private enforcement has encouraged sellers to adopt a position of \textit{per se} legality, including conservative pricing policies, vertical integration, uniform pricing, etc.

A defendant may acquiesce to the F.T.C. and accept a Consent Order prior to trial rather than run the risk of an unfavourable Court judgement which may be used against him in a private suit. In this way, private enforcement has the same effect as lowering the standards of injury, ie. it becomes easier for the F.T.C. to achieve compliance and therefore the Act further inhibits the pricing flexibility.

Private enforcement has also been used to bolster horizontal price fixing agreements\textsuperscript{61}. Sellers in an oligopolistic market characterised by excess capacity, seeing a rival firm making discriminatory discounts, have invoked the Robinson-Patman Act to prevent such pro-competitive pricing. Thus pro-competitive price discrimination has been stifled.

(4) \textbf{Current Trends in Enforcement}

In the 1970's the F.T.C. and Dept. of Justice have attempted to redirect their resources to more important areas of antitrust and to limit the anti-competitive effects of the Robinson-Patman Act. They have

\textsuperscript{60} Dept. of Justice Report, pp. 33-35.

\textsuperscript{61} This is not only true of private enforcement. For example, a concerted effort by carpet manufacturers to eliminate quantity discounts within the industry met with Sherman Act conspiracy charges from the Dept. of Justice. Years later, the same manufacturers negotiated Consent Orders with the F.T.C. under the Robinson-Patman Act to eliminate comparable discounts. Rowe, The Federal Trade Commission's Administration of the Anti-Price Discrimination Law, p. 427; Liebelier, \textit{op. cit.}, p. 30.
attempted to achieve these objectives simply by not enforcing the Act\textsuperscript{62}. However, the ill effects of the Act are still perpetuated by private enforcement which is outside the control of the F.T.C. and Justice Dept. The Justice Dept. has recommended that in the event the Robinson-Patman Act is retained, the right of private enforcement be removed\textsuperscript{63}.

4.8 REPEAL OF THE ROBINSON-PATMAN ACT

The Dept. of Justice Report identifies perhaps the most ironic aspect of the Robinson-Patman Act\textsuperscript{64}:

\ldots the actual impact of the 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 that it is obeyed, its effects are magnified.

\textsuperscript{62} These statistic's were issued by the Bureau of Competition of the F.T.C.

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<td>1978</td>
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Source: ABA Report, p. 41.

\textsuperscript{63} Dept. of Justice Report, p. 263-264.

\textsuperscript{64} Dept. of Justice Report, p. 38.
(1) The Act Promotes Price Rigidity and Inefficiency

It has been shown that the Act has many undesirable effects as it attempts to regulate the pricing process. The Act has promoted price rigidity and inefficiencies in complete conflict with antitrust principles.

This has occurred because sellers fear prosecution under the Act. Prosecution may be feared because of the ease of establishing a violation. The jurisdictional elements are clear-cut and easy to establish, the standards of competitive injury are low or non-existent in the case of brokerage and proportional allowances, and the defences are hard to prove. The continually shifting standards established by the F.T.C. and Courts have increased the difficulty of determining legality and finally the costs of prosecution are high in terms of legal costs, damages, and private costs.

Rather than risk a prosecution under the Act, sellers and buyers adopt a path of per se legality. This means conforming to the language and philosophy of the Act. A seller may adopt a one price system, cost-plus pricing, or he may meet but not beat the prices of competitors. Alternatively the seller may remove his pricing from the jurisdiction of the Act either by selling through agency agreements, differentiating products, refusing to supply some buyers, etc. Each of these choices leads to inefficiency.

The Act may be enforced by competitors of the seller who are

65 "The FTC itself, in recent years has de-emphasized formal proceedings enforcing the Robinson-Patman Act. In addition, many recent pronouncements by the FTC in the Robinson-Patman area have reflected increasingly sharp differences of policy among the Commissioners, with a multiplicity of opinions precluding any clear guidance to the meaning of the Act. There is now widespread uncertainty among businessmen and their advisors as to how to comply with this statute". Report of the ABA Committee to Study the F.T.C., Sept. 15, 1969, Reprinted in 1 Jnl. of Reprints for Antitrust Law & Econ. 859 (1969), p. 957.
motivated to eliminate the aggressive pricing practices of a strong competitor, and the meeting competition defence leads to industry-wide price rigidity and may allow inter-seller verification.

The cause of these problems is the basic philosophy of the Act. The Act promotes restrained pricing and can be seen as a regulatory rather than a pro-competitive statute. It rejects price discrimination and replaces it with price uniformity, cost-based pricing or discriminatory pricing which is essentially defensive. Both the seller and the buyer are discouraged from engaging in the normal bargaining process.

To the extent that the Act is ignored, the deleterious effects are minimised and the pro-competitive effects of price discrimination are attained. The regulatory bodies have recognised this by severely reducing their enforcement of the Act. The Courts have also recognised this and have raised the threshold standards of injury to exempt a higher proportion of discriminations from the ambit of the Act.

These bodies are in the peculiar position of suggesting that the Act best attains its goals of promoting competition and efficiency when it is made impotent. Almost all commentators have recognised the fundamental conflict between the Robinson-Patman Act and antitrust principles. This has led to calls to repeal or substantially amend the Act. Many of those who have called for the amendment of the Act have done so after recognising the difficulty of repealing the Act outright. The premises upon which the Neal Committee base their revision

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66 Rowe, Price Discrimination Under the Robinson-Patman Act, Chapter 17 and references cited p. 551 n. 68. Elman, op. cit.; Liebeler, op. cit; Neal Committee, the Nixon Task Force on Productivity and Competition, (the Stigler Report), 91.1617, 91st Cong. 2d Sess. 27 (1970); and see also the comprehensive list of references cited in the ABA Report, p. 21 n. 86.

67 The Attorney General's Committee; the Neal Committee; and the proposals of the Justice Dept., supra, n. 25.
are representative of this view\textsuperscript{68}:

1) There are many reasons for price discrimination and most of them are related to the improved functioning of the competitive system.

2) It is possible for price discrimination to adversely affect competition but such instances are exceptional.

3) A statute designed to restrict price discrimination must therefore be narrowly drawn, so that the important benefits of price discrimination will not be lost in an excessive effort to curb limited instances of harm.

4) Revision of the Robinson-Patman Act is preferable to its repeal, since repeal would not preclude the wholesale transfer of Robinson-Patman doctrine to sections 1 and 2 of the Sherman Act and section 5 of the Federal Trade Commission Act.

The Stigler Committee, a second Government body to heavily criticise the Robinson-Patman Act provides another reason for retaining the statute\textsuperscript{69}:

The Task Force recognizes the political support that the Robinson-Patman Act retains in some quarters and the danger that an attempt to amend the Act might give particular interests an opportunity to add even more restrictive provisions.

(2) \textbf{The Need for the Robinson-Patman Act}

The Robinson-Patman Act has had many undesirable effects on competition and efficiency and it has been suggested that these effects warrant repeal of the Act. To support the call for repeal it is argued that the Robinson-Patman serves no useful purpose. Thus it is not a case of balancing the pro's and con's of the Act — there are only con's.

The objectives of the Act are:

(i) to prevent predatory pricing,

(ii) to prevent monopoly in the channels of distribution,

(iii) to promote the interests of small business.

\textsuperscript{68} Neal Report, C-1.

(a) Preventing Predatory Pricing. The Act is not necessary to prevent predatory pricing. This conclusion is derived directed from the findings that a) predatory pricing is not common, and b) the Sherman and Federal Trade Commission Acts already provide adequate protection against this practice.

Studies conducted by academics and Government bodies have concluded almost unanimously that predatory pricing is rarely if ever practiced70. By prohibiting price discrimination causing primary line injury, the Act has done more to prevent pro-competitive price discrimination, (ie. promotional pricing or price discrimination to test market conditions), than it has to prevent predation.

Even if predation were a major concern, (and it is not suggested that it is), the provisions of the Sherman Act and the Federal Trade Commission Act are better suited to deal with the problem. The Robinson-Patman Act treats price discrimination as though it were the problem. It fails the recognise that the problem is the monopoly structure in the industry. The anti-monopoly provisions of the Sherman Act provide a more effective recourse against the monopolist than does the Robinson-Patman Act.

In defence of the Act some supporters argue that the Act has a lower threshold test for injury. We have seen, however, that the Courts have equated the Sherman Act and Robinson-Patman Act tests71, and that the effect of the lower test was to prevent pro-competitive pricing.

70 Banta & Field, op. cit., pp. 107-108; Dept. of Justice Report, pp. 164-168; and authors cited, supra, p. 26 n. 18, p. 27 n. 20.

71 See Hovenkamp, Judicial Reconstruction of the Robinson-Patman Act: Predatory Differential Pricing, 17 UCD Law Review, 309 (1983), at pp. 323,324. Some supporters of the Act point out that the Sherman Act requires the monopolist to have 'a dangerous degree of success' before the Act is applied and that this distinguishes the two Acts. If this is so, then it seems to support the argument for repeal of an Act when penalises a monopolist even though he has no possibility of success.
There is no strong argument either for a Robinson-Patman Act that duplicates the Sherman Act, or for a Robinson-Patman Act that employs a low injury standard.

(b) Preventing Monopoly in Distribution. An additional goal of the Robinson-Patman Act is to prevent monopoly in distribution. To achieve this goal the Act has attempted to give a monopoly position to the wholesaler, the broker and the small retailer by insulating them from competitive pressures of new forms of distribution. However, the Act has not achieved this goal and it would be more correct to say that the Act has simply slowed the growth of more efficient forms of distribution.

The Act has not been successful in limiting excessive discounts to large buyers. The buyer may receive discounts by\(^{72}\):

(i) taking a sellers entire output at a low price,
(ii) obtaining low prices from a seller meeting the competition of another,
(iii) buying goods cheaply abroad,
(iv) buying physically and brand differentiated products,
(v) obtaining goods of premium quality at non-premium prices,
(vi) producing the goods itself,
(vii) obtaining the goods at a low price using a long term contract,
(viii) integrating vertically,
(ix) receiving secret concessions and rebates.

The availability of these options suggest that the Act cannot be used to prevent discounts being granted to the large buyer. Indeed, a perusal of these options shows that most of them are legal means of obtaining lower prices.

Nor is the Act necessary to prevent monopoly in distribution. The injury caused by discriminatory discounts is usually very small and one would expect it to occur over a very long period of time, yet there are many other forces determining the success or failure of competitors in the market and in the long run these other forces will have a greater impact on the distribution channels than discriminatory discounts.

The small buyers may be protected by the seller. The seller has a vested interest in the welfare of his customers as he depends upon them to distribute his product. In the absence of these buyers, the seller would find himself at the mercy of the buyer who tries to use his countervailing power to secure some of the monopoly profits available to the seller. Thus, the growth of monopoly at the distribution level would be totally contrary to the long-term interests of the seller. (It might also be contrary to the interests of the large monopolist to totally control distribution channels as this would attract more stringent anti-monopoly measures from Congress. The monopolist is better served by enjoying the 'quiet' life).

One can also ask whether we should fear the possibility of monopoly in the channels of distribution. The ease of entry and exit suggests that no firm could achieve sufficient monopoly power to affect prices (which is the definition of monopoly). If a firm raised prices he would quickly encourage new entrants into the market. Thus there are considerable latent forces controlling the monopolist-distributor.

(c) Protecting Small Business. Nor can the Act achieve its third objective of promoting small business. The Dept. of Justice Report provides arguments that illustrate that the Act cannot materially affect the success or failure of small business and, in many cases, the Act may

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even inhibit the growth of small business. If small business is seen as a desirable objective then it should be attained by direct rather than indirect means.

Small business usually competes with larger business in terms of service. Although their prices are usually higher than the chain store, the small business retains his market position by offering longer trading hours, personal service, greater specialisation, an image of 'quality', etc. The success or failure of small business depends upon the consumer's preference for these types of services over the low-price appeal of chain-stores. Price differentials granted to the larger firms do not significantly alter the competitive position of the small buyer.

The resort to service competition is only one of the ways in which small business has reacted to the competitive pressure of chain stores. Small businesses have combined to form co-operatives enabling them to by-pass the traditional intermediaries such as the wholesaler, broker, etc, and to receive discounts for quantity and volume of purchases. However, the Robinson-Patman Act has prevented sellers from granting functional discounts (especially brokerage), and quantity and volume discounts to the co-operatives. Also the F.T.C. has shown that it is prepared to enforce the Act vigorously against co-operatives.

The Robinson-Patman gives minimal, if any, protection to small businesses and if small business failure did reach epidemic proportions, assistance should be direct and open rather than indirect and disguised as an antitrust statute. Tax concessions and small business incentives are a more effective means of assisting small business.

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(3) **Conclusion**

Price discrimination legislation similar to the Robinson-Patman Act is not desirable as it interferes with the pricing flexibility of the seller. This is both anti-competitive and inefficient. Nor does such legislation achieve the goals for which it was enacted. These goals can be attained by alternative means.

Many of those commentators who recommend revisions of the Act propose that the impact of the Act on pricing decisions be lessened. To this end recommended changes are the raising of threshold injury tests (especially at the primary level), injecting greater flexibility into the defences, repealing the *per se* provisions, the Quantity Limits proviso and the criminal provisions, and limiting the effect of private enforcement either by restricting private enforcement itself or denying the opportunity to receive treble damages.

However, these recommendations are made in light of the general conclusion that as the Act becomes more stringent its detrimental effect on pricing (and hence on competition and efficiency) increases also. This cannot be rectified by slight modification to the Robinson-Patman Act. The problems are fundamental - the assumption that prices are based on costs, the intra-industry price matching that results from the meeting competition defence, the restraints which limit the normal competitive bargaining process between sellers and buyers, the necessarily low secondary line injury criteria, and the difficulty of distinguishing between pro- and anti-competitive price discrimination. These problems are inherent in any anti-price discrimination law and cannot be eradicated by legislative amendment.
CHAPTER V

THE AUSTRALIAN APPROACH TO PRICE DISCRIMINATION

5.1 THE TRADE PRACTICES ACT 1974: SECTION 49

(1) Introduction.

The Australian law relating to price discrimination is contained in the Trade Practices Act 1974. Section 49 deals directly with price discrimination, while Section 46 condemns the abuse of market power and Section 45 makes unlawful contracts, arrangements and understandings in restraint of trade.

Section 49 of the Trade Practices Act is modelled on the Robinson-Patman Act, although modified in an attempt to avoid many of the shortcomings of that Act. This section provides a unique opportunity to consider the effectiveness of a modified Robinson-Patman Act in an economy that is similar to that of New Zealand in terms of industrial concentration. Section 49 provides:

(1) A corporation shall not, in trade or commerce, discriminate between purchasers of goods of like grade and quality in relation to-
   (a) the prices charged for the goods;
   (b) any discounts, allowances, rebates or credits in relation to the supply of goods;
   (c) the provision of services in respect of the goods; or
   (d) the making of payments for services provided in respect of the goods,
   if the discrimination is of such magnitude or is of such a recurring or systematic character that it has or is likely to have the effect of substantially lessening competition in a market for goods, being a market in which the corporation supplies, or those persons supply goods.

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(2) Sub-section (1) does not apply in relation to a discrimination if -
   (a) the discrimination makes only reasonable allowance for differences in the cost or likely
cost of manufacture, distribution, sale or delivery resulting from the differing places to
which, methods by which or quantities in which the goods are supplied to the purchasers; or
   (b) the discrimination is constituted by the doing of
an act in good faith to meet a price or benefit
offered by a competitor of the supplier.

(3) In any proceeding for a contravention of sub-section (1),
the onus of establishing that sub-section (1) does not
apply in relation to a discrimination by reason of sub-
section (2) is on the party asserting that sub-section
(1) does not apply.

(4) A person shall not, in trade or commerce -
   (a) knowingly induce or attempt to induce a
corporation to discriminate in a manner
prohibited by sub-section (1); or
   (b) enter into any transaction that to his knowledge
would result in his receiving the benefit of a
discrimination that is prohibited by that sub-
section.

(5) In any proceeding against a person for a contravention of
sub-section (4), it is a defence if that person
establishes that he reasonably believed that, by reason
of sub-section (2), the discrimination concerned was not
prohibited by sub-section (1).

Section 49 may be enforced by the Trade Practices Commission or
privately through civil damages suits. A contravention of section 49 may
result in pecuniary penalties, injunctions, ancillary orders, or, in
private cases, an award for damages. Unlike some other sections of the
Act, the authorisation process is not applicable. The authorization
process seeks to reduce uncertainty and ensure that businesspeople are
not deterred from entering contracts that enhance competition by
allowing such people to apply for authorization of the trade practice
irrespective of the provisions of the Trade Practices Act. Because the
process is not applicable to Section 49, a discriminating seller cannot
avoid the uncertainties of the section.
(2) Enforcement of Section 49

Unfortunately there has been a dearth of cases brought under this Section. One reason is that the Trade Practices Commission has preferred to direct their limited resources to practices which have a more serious effect on competition, such as resale price maintenance and exclusive dealing. Although the Commission indicated in 1977 that it intended to develop a program to monitor the existence and effect of price discrimination in a number of selected areas, it still did not instigate any cases itself. The reasons for this are outlined in their (1979) Fifth Annual Report:

There have been no Commission proceedings in Court, and no private actions have come to hearing. The Commission has received since the Act commenced some 180 complaints about alleged price discrimination, with well over half coming from individual small businesses who typically believe that a larger outlet nearby is getting a better deal from a common supplier. Often the suspicion of the better deal in purchase is brought about by the larger outlet selling at lower prices. The complaints have come from the full range of typical small businesses. Sometimes quantity discounts do not appear to be out of line with likely economies of fewer deliveries and larger drops per delivery. Sometimes the particular market appears to be such that competition is unlikely to be substantially lessened which is a requirement before the section is breached. Most of the complaints were not taken any distance because on the facts available there appeared to be no chance of their coming within section 49. Some were really complaints about the presence of competition.

Hence no cases have been brought by this Authority and the only case to be fully considered by the Federal Court originated from a private action.

(3) A Comparison of the Robinson-Patman Act and Section 49

Most commentators agree that much of the American case law is directly relevant to interpreting the Australian section because of the close similarity between the Robinson-Patman Act and Section 49 of the

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2 Trade Practices Commission, Fifth Annual Report - Year ended 30 June 1979, Para. 5.2
Trade Practices Act. Not only is the structural approach of the two provisions identical, but in recent times, U.S. Courts have given a stricter interpretation to the Robinson-Patman Act which conforms more closely to S. 49 than a simple comparison of the wording would first suggest. There is one difficulty with applying American interpretation en masse to Section 49 and that is U.S. Courts have been willing to interprete the Robinson-Patman Act in such a way as to achieve the legislative objectives of the Act. By comparison Australian Courts have not conjectured on the intentions of the legislators but rather interpreted the Act strictly according to the wording.

The major differences between the two price discrimination statutes are that the Australian Act employs a higher threshold test for injury, there is no specific provisions for indirect forms of price discrimination in Section 49, and the burden of proof in buyer liability cases differs.

(a) A Higher Standard of Competitive Injury. For a discrimination to violate Section 49, the plaintiff must show that it is "of such magnitude or is of such a recurring or systematic character that it has or is likely to have the effect of substantially lessening competition in a market for goods, being the market in which the corporation supplies, or those persons supply, goods". Thus, there is an additional jurisdictional element relating to the size and systematic nature of the discrimination. This was inserted to ensure that only anti-competitive (ie. systematic) price discrimination was made illegal. Blakeney


4 Eg., see R. B. Sharpe, When is a Purchaser not a "Purchaser"?, 49 Law Institute Journal 370 (1975), p. 371.
writes:

It is questionable whether these words add much to the sub-section, as minor, episodic or haphazard discriminations are unlikely to produce a substantial impairment of competition. This form of words may, however, serve four purposes: first, it indicates that pro-competitive sporadic and unsystematic price discrimination is to be preserved from prohibition. Secondly, it may serve as an indication to the courts that Parliament did not wish trivial discriminations to be taken into account. More usefully, it could have been inserted as a guide to the courts as to when the likelihood of anti-competitive harm could be inferred. Finally, the disjunction of "magnitude" and "recurring or systematic" distinguishes S. 49(1) from the Robinson-Patman case law which seems to insist upon both a systematic pattern of price discrimination which is substantial in amount.

Section 49 contains no mention of adverse effects on competitors and thus there is not the same protectionism implicit in the Robinson-Patman Act. The Section 49 test requires the injury to competition to be "likely" and not merely "reasonably possible". And the injury must "substantially lessen competition". Pengilley notes:

It is tempting to regard the term "substantial" as contemplating some quantitative market share (i.e. competition is reduced by x% or x% of competition is foreclosed) and then run an evaluation as to whether the relevant percentage is or is not "substantial". Australian interpretation has, however, not embraced this approach. So, "substantial" has been regarded as being "real or of substance and not insubstantial or nominal" - an approach which does not equate to the quantitative substantiality approach.

Each of these suggests that a plaintiff must provide a higher standard of proof to establish competitive injury under S. 49 than would be required under the Robinson-Patman Act. The Australian section is concerned more with competition than individual competitors and is less likely to have the unanticipated detrimental results that plagued the


6 Pengilley, op. cit., p. 31, (Footnote omitted).
Robinson-Patman Act.

One notable feature of the competitive injury test contained in Section 49 is that it is confined to primary and secondary line injury. Tertiary line injury is omitted.

(b) Absence of Provisions For Specific Forms of Discrimination. The main provisions of S. 49 relate to indirect as well as direct price discriminations. The same competitive injury test and defences are applied to all discriminations, regardless of whether the discrimination takes the form of discounts, allowances, rebates, brokerage, or the provision of promotional services and allowances.

(c) Reallocations of the Burden of Proof in Buyer Liability Cases. The burden of proof in buyer liability cases differs between the two provisions. Under Section 49, the buyer must show that it was reasonable for him to rely on the cost justification and meeting competition defences, whereas under the Robinson-Patman Act it is incumbent on the plaintiff to prove that such defences were not available to the seller and that the buyer reasonably knew this.

(4) Australian Judicial Interpretation. Section 49 has not received sufficient judicial attention to accurately judge the significance of these changes. Of special interest is the impact of the new competitive injury test. Possibly the higher standard applied in recent U.S. cases (especially primary line cases), and the minor impact of the additional terms "recurring or systematic" and "substantial" will mean that the U.S. and Australian tests are very similar.

Only one case has been decided to clarify the meaning of Section 49. That case, Cool & Sons Pty. Ltd. v. O'Brien Glass Industries Ltd\(^7\),

involved the use of price discrimination to enforce exclusive dealing and resale price maintenance. Cool was one of two major retailers and fitters of replacement windscreens to the public. The other was O'Brien, a vertically integrated firm that also supplied windscreens to the area. O'Brien did not hold a monopoly in the supply of windscreens and competed with three other suppliers. Only at the beginning of their operations did Cool buy a majority of their windscreens from O'Brien. O'Brien had a practice of granting a 50% discount if the buyer brought all or substantially all of their supplies from O'Brien. Cool failed to do this and their discount was reduced to 40%. Discounts were also refused to Cool because of their discounting practices.

The case covered issues of resale price maintenance, exclusive dealing, and price discrimination. Unfortunately the judgments of the trial judge and the Full Court either did not elaborate on their findings or confused the issues of exclusive dealing and price discrimination. There seemed little question that Cool was discriminated against because of their buying and discounting practices and contraventions of S. 47 and S. 48 were found.

The question was whether this discrimination was contrary to S. 49. In particular, whether the discrimination substantially lessened competition in the market, defined as the Wagga retail market for replacement windscreens, which included Wagga and the area within a 50 mile radius. Keely J. at first instance, found an offence as a matter of fact. On appeal to the Full Court, Sheppard J. indicated that where a seller discriminates between two competing buyers "there will almost always be a substantial lessening of competition in a relevant market"

(footnote cont. from p. 272)
(before Keely J. when injunction sought to be lifted. This motion denied); O'Brien Glass Industries Ltd. v. Cool & Sons Pty. Ltd. [1983] ATPR 40-376 (Full Federal Court Of Appeal - Fox, Franki and Sheppard JJ.). appealed 48 ALR 625
ie. "the market in which the two purchasers themselves supply goods"\(^8\), while in dissent Franki J. found that adequate competition existed despite the granting of discriminatory terms in the market\(^9\). Hence no clear dictum exists relating to the standard of competitive injury necessary to establish a violation. Pengilley writes\(^{10}\)

All judgments (other than that of Franki J.) would seem to contemplate the possibility that price differentials between purchasers may of themselves be anti-competitive and this may be quite close to holding discrimination per se illegal.

The Federal Court decision has set "business adrift on the sea of commerce without a buoy let alone a beacon with which to assist or guide its conduct"\(^{11}\).

(3) Evaluation of Section 49

(a) The Swanson Committee. Section 49 has received the same criticisms as the Robinson-Patman Act. Among those arguing for repeal are two government committees established to investigate the working of the Trade Practices Act 1974.

In 1976 the Trade Practices Act Review Committee, (the Swanson Committee) was established. Paragraph 4 of its terms of reference directed it to consider the operation of the substantive prohibition of the Act relating to restrictive trade practices, with close attention to exclusive dealing, price discrimination, mergers, etc, and especially, in relation to price discrimination, if it is appropriate for the Act to have regard to anti-competitive effects in the buyer's market, or in any other market other than the seller's.

Despite this reference which seems to suggest the strengthening of

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\(^{8}\) [1983] ATPR 40-376 at p. 44,472.  
\(^{9}\) [1983] ATPR 40-376 at p. 44,467.  
\(^{10}\) Pengilley, op. cit., p. 39.  
\(^{11}\) Pengilley, op. cit., p. 56.
the Act by removing the secondary line competitive injury requirement, the Committee recommended the outright repeal of the section. It pointed to the submissions of small business groups who, "with two notable exceptions, thought the section had either worsened the relative position of small business or not assisted them in any way." 12 Other submissions referred to the negative impact of the section on pricing flexibility 13. Thus 14:

The Committee considers that in the Australian context the conduct of a large buyer who is endeavouring to secure price cutting in his favour, whether it be discriminatory or not, may be more pro-competitive than anti-competitive. Indeed, such price cuts as a large buyer is able to obtain can trigger off competition from rival suppliers or can trigger off competition in a market, where other forces are unlikely to produce active competition.

...the prohibition on price discrimination in Section 49 has, in our view, operated substantially to limit price flexibility. The Committee believes that in the Australian context, section 49 has produced such price inflexibility that the detriment to the economy as a whole from the operation of the section outweighs assistance which small business may have derived from it. It is price flexibility which is at the very heart of competitive behaviour. The Committee thus recommends that Section 49 should be repealed.

The Swanson Committee support their recommendation with both theoretical objections and market experience in the form of submissions.

The recommendation was originally accepted by the Liberal/Country Party Government in the proposed Trade Practices Amendment Bill submitted in December 1976. However, the first amending Bill lapsed with the prorogation of Parliament in February 1977, and the clause deleting Section 49 was not included in the second amending bill introduced in May 1977. The protection of small business was given as the reason for

13 ibid., para. 7.3.
14 ibid., para. 7.20,7.21.
the retention of the section\textsuperscript{15}.

(b) The Blunt Committee. In 1978 the Government directed the Trade Practices Consultative Committee, (the Blunt Committee), a body established to advise the Minister for Business and Consumer Affairs on the operation of the Trade Practices Act, to report on the impact of the Act on small business. Included in the terms of reference was this statement:

Consistent with the general objective of the development and maintenance of free and fair competition in the Australian economy, is there any action in relation to the Trade Practices Act 1974 which your Committee considers should be taken, with the objective of the improvement of the market position of small business in Australia. Particular attention should be had to the provisions of the Act dealing with monopolization (section 46), exclusive dealing (section 47), price discrimination (section 49) and relevant ancillary provisions.

In developing a framework in which to evaluate section 49, the Committee saw the promotion of competition and efficiency as the objectives of the Act\textsuperscript{16}:

10.36 ...we see that the immediate objective of the competition rules of the Act is the minimisation of conduct which works against the efficient allocation of resources. The general principle adopted is that it is the market place which allocates resources and not sectional interests. We think the primary thrust of any price discrimination law should be towards the promotion of efficiency in firms through the elimination of anti-competitive behaviour. While a price discrimination law may be directed at protecting small businesses this should not be at the expense of efficiency.

10.50 While section 49 would appear to be consistent with the general policy of the Trade Practices Act, the operation of that section has achieved results which are not easily reconciled with other specific measures adopted under the Act.

10.51 After section 49 came into operation, in February 1975,

\textsuperscript{15} See Pengilley, \textit{op. cit.}, Appendix A.

the following, possibly short-term, effects upon price levels in various industries were noted. Either:

- discounts were eliminated altogether, with uniform prices becoming the pre-discount level, the consequences being a net price increase; or
- discounts were eliminated altogether but uniform prices were set at a level to provide the seller with the same net return; or
- discounts were largely eliminated for the small, medium and medium to large enterprises with discounts being available only to large and very large enterprises, often on a secret basis.

The Committee also notes the possibility of anti-competitive price exchanges resulting from the operation of the meeting competition defence.\(^{17}\)

In relation to small business, the Committee notes that some submissions to the Committee reflect the view that the section is essential to the survival of small business. However, the Committee employs two arguments to support their case for repeal of the Section. First, the presence of discounts related to the size of the firm provides an incentive for small business to grow.\(^{18}\) This fosters competition in the long-term. Second, the Committee accepts those views expressed in the U.S. Dept. of Justice Report on the Robinson-Patman Act that the success or failure of small business is not determined by the existence of anti-price discrimination legislation but rather by consumer preference for the special services and facilities offered by small business.\(^{19}\)

The Committee rejected any attempt to strengthen S. 49 by removing the requirement for proving secondary line injury.\(^{20}\) Instead it canvassed two alternative solutions to the problem of Section 49. The

\(^{17}\) Blunt Committee Report, para. 10.53, 10.54.

\(^{18}\) ibid, para. 10.98, although the Committee did note that not all small businesses had the access to capital, the storage facilities, or the advertising funds to take full advantage of these opportunities.

\(^{19}\) ibid, para. 10.99.

\(^{20}\) ibid, para. 10.48 and para. 10.100.
first was a notification system to reduce the uncertainty of the section and thereby give sellers greater security when granting discounts to large buyers. The difficulty with this approach was that most price discriminations do not affect competition and hence the enforcement agency will be overloaded causing a major diversion of resources away from other, more important, areas of antitrust enforcement. Moreover the task of assessing anti-competitive effect under section 49 is more onerous than other practices where notification is allowed.

The second alternative was to repeal section 49. This solution, in conjunction with the strengthening of Section 46, which deals with the abuse of market power, was adopted by the Committee.

(c) Other Objections of Section 49. Criticism of this section has also come from academic circles and represents the view that the minor amendments that distinguish Section 49 from the Robinson-Patman Act are not sufficient to ameliorate the inefficient and anti-competitive effects of price discrimination law. In fact, the concentrated nature of the Australian economy may aggrevate the problems caused by price discrimination legislation. Professor Breyer considers the impact of price discrimination legislation in a concentrated economy:

Price discrimination is likely to pose a problem only when the selling market is highly concentrated, for firms in other highly competitive industries are less likely to be able to raise any of their prices above a uniform level approximating cost. Moreover, the more concentrated

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the industry in an economy, the more harm that can be
done by a rule against price discrimination.

For these reasons a strict interpretation of s. 49 is
likely to prove particularly harmful in Australia. Since
Australian industry is highly concentrated, the net
effect of preventing price discrimination is more likely
to be uniformly high prices rather than uniformly low
ones.

Another undesirable effect of the section on the Australian
economy is that manufacturers may not be able to effectively compete
against imports if they are forbidden to adjust their price to meet
competition. (There is, of course, the meeting competition defence,
however, the uncertainties surrounding the application of S. 49 and that
particular defence may discourage flexible pricing).

(4) The Response to Criticism of Section 49: The Proposed
Amendments to Strengthen the Section

The recommendations of the Swanson and Blunt Committees have not
been accepted by either of the two main political parties. The
Opposition Liberal/Country Party has affirmed their intention to retain
the section and has since enacted strict anti-price discrimination
provisions in the petroleum industry. The current Labor Government has
maintained their support for the section and even suggested
strengthening the provisions. The purpose is to make the Section more
effective and thereby of greater assistance to small business. The
proposals were part of a draft bill released on 21 February 1984. They
include:

(i) The lowering of the threshold competitive injury test by
removing the requirement that the competitive injury be substantial.
Alternatively, the competitive injury clause could be amended to prevent
a discrimination if "it has or is likely to have the effect of
substantially lessening the competitiveness of the business or
businesses being discriminated against in a market for goods..."
(ii) The provisions would be extended to cover potential purchasers, defined under a new subsection, section 49(6), as "a person who has entered into negotiations with respect to the purchase of the goods."

(iii) An availability defence would be inserted which would allow price discrimination where the buyers have access to goods of like grade and quality at a comparable price from a source other than the supplier.

(iv) Penalties would be doubled from $250,000 per offence to $500,000 per offence.

(v) The cost justification defence would be widened. One suggested method of making the defence more flexible would be to remove the term "only due allowance" from the text, thereby releasing the party asserting the defence from a requirement of mathematical precision.

The addition of the availability defence and the attempt to add flexibility to the cost-justification defence would be welcome measures if the section is to be retained.

The other amendments, extending the jurisdiction, lowering the threshold test for injury and increasing the penalties, are more controversial, especially in light of the stated objective of giving greater protection to small business. Widening the scope of the section to include potential purchasers may bring greater caution in bargaining and thereby increase the price rigidity caused by the section. In addition there is the problem already cited of determining when a seller and buyer enter into negotiations. This provision may deter any bargaining in the market place.

Increasing the penalties might bring a concurrent increase in the standard of proof necessary to establish a violation contrary to the objective of making the section more accessible to small business. It may also make large sellers more reluctant to grant discounts and hence
aggregate the anti-competitive tendencies of the section.

The most serious proposal is the lowering of the threshold competitive injury test either by removing the substantiality requirement or by refocussing the test on injury to competitors rather than competition. The anti-competitive effects of lowering the standards can already be seen in cases such as Utah Pie and the Automotive Parts cases where pro-competitive conduct was prevented because it harmed individual competitors. The reader is reminded of the words of Corwin Edwards quoted earlier that successful competition necessarily harms competitors, and that individual competitors can be protected only at the expense of the competitive process itself.\textsuperscript{23}

Dr. Pengilley criticises the Attorney General's reasons for strengthening the section.\textsuperscript{24} The Attorney General's complaint that there has only been one successful case under the Act, Pengilley claims, does not warrant lowering the standards to ensure more successful cases. Looking solely at the number of successful cases brought under the Section gives no indication whether the section has successfully curbed anti-competitive price discrimination. In fact, the lack of cases may indicate that the section has been particularly successful in achieving that objective. Pengilley also points out that the proportion of private complaints brought under section 49 exceeds that brought under either section 47 or section 48. In addition, enforcement of the section has been by means other than legal proceedings and Pengilley points to the facts relating to Pilkington ACI's discriminatory pricing policies, which were substantially revised following complaints by the Trade Practices Commission.

\textsuperscript{23} See Edwards, quoted supra, p. 78.

\textsuperscript{24} Pengilley, Handbook on Price Discrimination: The Present Position and the Impact of Legislative Proposals, pp. 74-75.
Encouraging the Trade Practices Commission to bring more cases under section 49 may have other deleterious effects. Resources may be diverted from more important areas such as Resale Price Maintenance and Exclusive Dealing. The lack of enforcement by the Trade Practices Commission merely shows that "it has chosen to act in an area where there are wider repercussions for competition policy generally.\(^{25}\) To force the Commission to get a "successful case" may force the Trade Practices Commission to ignore its responsibilities in other areas of competition policy.

A second justification for the proposed amendment to the competitive injury clause is that a small business may be harmed by discriminatory pricing even though overall competition has not been impaired. By lowering the threshold injury test, the section is made more accessible to small business. In response, Pengilley considers that current low standards found in many Trade Practices Commission decisions, the low standard used in *Cool v. O'Brien*, and the amendment to the merger provisions to provide for a more substantial market, indicates that injury to competition is easy to prove and this should provide adequate protection for small business. Nor does Pengilley agree that the section assists small business in the first place.\(^{26}\) Pengilley considers that the Australian section will have the same impact on small business as the Robinson-Patman Act; that is, it encourages vertical integration and agency agreements, it encourages one-price pricing systems, it encourages sellers to supply to only one level of distribution or to only one type of buyer, it discourages the growth of buying co-operatives, and prevents sellers from reimbursing small

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retailers for the extra costs of distribution. All of these consequences may harm small business.

Pengilley concludes27:

The most obvious thing about Section 49 is the complete absence of any demonstrated need to amend it. Indeed, the available material indicates that repeal may be desirable leaving the Section 49 functions to be taken over by Section 46 or a suitable redraft of that section.

5.2 ALTERNATIVE CONTROLS ON PRICE DISCRIMINATION

The Australian Trade Practices Act 1974 contains several alternative means of attacking price discrimination. Chiefly, section 46, outlawing the abuse of a dominant market position, can be used to prevent predatory conduct. Also there are provisions governing refusals to deal and discriminatory dealing when used to enforce exclusive dealing and resale price maintenance. Section 45 relating to anticompetitive agreements can be invoked if the price discrimination arises out of a contract, arrangement, or understanding between firms. Finally, in response to complaints of discrimination in the petroleum industry, the Petroleum Retail Marketing Franchise Act 1980 was enacted to ensure all franchised dealers received equal treatment.

(1) Section 46: The Monopolization Provisions

Section 46 outlaws the abuse of a dominant market position. (It is noted that it does not attack the achievement of that position in the first place, nor does it prohibit mere size). The section is breached where:

(a) A corporation is in a position substantially to control a market for goods or services;

(b) the corporation takes advantage of the power that it has by virtue of being in that position in the market;

(c) the conduct is undertaken for the purpose of eliminating or substantially damaging a competitor in any market, or preventing the entry of a person into any market, or deterring or preventing a person from engaging in competitive conduct.

Although seen as generally suitable to deal with the problems of monopolisation, there have been some suggestions for strengthening the section. The amendments aim to lower the threshold requirement of market power by replacing "A corporation that is in a position substantially to control a market" with "A corporation that has a substantial degree of market power", and to capture conduct where the effect, but not necessarily the purpose, is to hinder competition.

(a) "Substantially to Control a Market". The meaning of this term is further clarified in Section 46(3),(4):

(3) A reference in this section to a corporation or other body corporate being in a position substantially to control a market for goods or services includes a reference to a corporation or other body corporate, as the case may be, having, by reason of its share of the market, or its share of the market combined with the availability to it of technical knowledge, raw materials or capital, the power to determine the prices, or control the production or distribution, of a substantial part of the goods or services in that market.

(4) A reference in this section to substantially controlling a market for goods or services shall be construed as a reference to substantially controlling such a market either as a supplier or as an acquirer of goods or services in that market.

The purpose of the proposed amendment is explained in the Report of the Blunt Committee:

9.23 In our view, unilateral predatory conduct should clearly be brought within the scope of section 46 if it is engaged in by any firm abusing any substantial degree of market power. The present words "substantially to control

28 Blunt Committee, pp. 69-70.
a market for goods or services" have on one view of their
definition as set out in sub-section 46(3) been written
down so as effectively to lower the threshold of firms
which are subject to scrutiny under Section 46 to include
most firms in particular markets which do have
substantial market power. However, we have the clear
impression that many people, including some who seek to
enforce the Act, tend to interpret the words and their
definition as only proscribing purposive conduct by the
market leader. If this interpretation were correct the
section would not be effective to curtail the predatory
actions of other powerful firms, in a market, which are
directed at smaller firms. In any event we think that
these doubts as to the limited class of firms to which
section 46 has application are the main reason why the
section has not been the subject of much litigation.

9.24 We think that if the words "in a position substantially
to control a market for goods or services" were replaced
by the words "that has a substantial degree of market
power" the direction of the section's thrust would be
clearer. We would also recommend certain other
consequential changes and an amendment which would make
it clear that it is not normal or even fierce competitive
rivalry between firms of comparatively equal strength
which it is sought to contain but rather the predatory
acts of powerful firms against smaller firms.

9.25 If the changes we suggest are made, Section 46 should be
less ambiguous and should clearly be able to be used by
victimised smaller firms in preventing predatory conduct
engaged in against them by medium as well as large firms,
whilst at the same time ensuring that normal competitive
behaviour, particularly between firms of equal market
power, is not affected.

After reviewing the relevant case law, Mr. Brian Wilson finds
that there has seldom been any difficulty in establishing that a firm
has the degree of market power required by the present wording.29 This

29 B. Wilson, The Changes to Section 46: Their Effect on Large
Participants in Australian Markets, a paper given as part of a seminar
etitled The Proposed Trade Practices Amendments: Their Legal and
Economic Impact, conducted by the Business Law Education Centre, Sydney
22 March 1984, Melbourne, 23 March 1984, p. 9. Referring to the cases of
Top Performance Motors Pty. Limited v. Ira Berk (Queensland) Pty.
Pty. Limited, [1980] ATPR 40-155, Wilson writes "In each of these cases
the Court found the threshold requirement of S. 46 easy to apply to the
respondent. However, the assumption of market control may not have been
warranted having regard to the generally accepted concepts involved in
market definition which, if applied to the facts of each of these cases
may have led a Court to determine that a proper market was much broader
and hence the Respondent could not be said to be in a position to
substantially control that market, making s. 46 relevant to its
(footnote cont. p. 286).
conclusion applies even after the meaning of 'market' was more broadly defined to include all close substitutes. Nevertheless he accepts the desirability of lowering the threshold test to ensure that anti-competitive conduct by any firm with market power is caught under the Act.

(b) "take advantage of". The difficulties of this part of the section can best be shown by reference to the facts in Top Performance Motors Pty. Limited v. Ira Berk (Queensland) Pty. Limited. Ira Berk was a sole distributor of Datsun motor vehicles in Queensland. One of its customers was the retail dealer, Top Performance. Ira Berk also retailed the vehicles in competition with Top Performance. The case arose after Top Performance sought to obtain an injunction restraining Ira Berk from terminating its dealer franchise. Ira Berk claimed the reason for the termination was dissatisfaction with the organisation and performance of Top Performance as a franchise dealer, and therefore the termination was for legitimate business reasons. The Court easily found that Ira Berk was in a position to control the market, however, they concluded it did not take advantage of that power when terminating the dealership, but rather was merely exercising its contractual rights.

The Blunt Committee, who recommended the strengthening of Section 46, argue:

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(footnote cont. from p. 285). In Top Performance Motors Pty. Ltd. v. Ira Berk (Queensland) Pty. Ltd., the court ruled that to control the supply of Datsun cars was "substantially to control a market for goods" within the meaning of Section 46. The Court stressed the differences between various brands of cars and thereby narrowed the product market from all cars to Datsun cars.


32 Blunt Committee Report, p. 70.
In our view these words, "taking advantage of the power", mean "use market power"; that is, the overt deliberate exercise of market power. To avoid confusion and misunderstanding we recommend that the word "use" replace "take advantage of".

(c) Purpose or Effect. A more intense argument is likely to develop over whether section 46 should proscribe conduct where the purpose of such conduct is to limit competition, or whether such conduct should also be proscribed where its effect is anti-competitive even though its purpose may not be. Arguments for such an amendment may be found from the failure of the Courts to proscribe conduct that hinders competition. Some cases illustrate this point.

In Ausfield Pty. Limited v. Leyland Motor Corporation of Australia Limited the respondent was the supplier of motor vehicle parts and accessories to Ausfield. The Federated Storemen and Packers Union of Australia, because of their dispute with Ausfield, placed a ban on the handling of Leylands goods which was lifted only after Leyland agreed not to supply parts and accessories to Ausfield. Leyland acceded because of the far-reaching financial impact that such a ban would have on its operations. It stressed that this was the reason for discontinuing supplies to Ausfield.

Ausfield commenced an injunction against Leyland to prevent this boycott, charging that the conduct breached ss. 45 and 46 of the Trade Practices Act. Mr. Justice Franki took the view that Leyland did not mean to harm Ausfield or prevent it from engaging in competitive behaviour, and accepted that its motivating purpose was to protect its own position - a legitimate business practice.

Two cases where there was arguably some predatory activity may be contrasted to show the weaknesses of S. 46 as a form of control of predatory activity. In Victorian Egg Marketing Board v. Parkwood Eggs

**Pty. Ltd**\(^{34}\) the appellant Board was a statutory authority and acquired all eggs produced in Victoria by statutory authority. It was therefore the principal wholesaler of eggs in that state. The Board was concerned with the entry into the Victorian egg market of the Bartters group of companies, (one of which was Parkwood) and, in retaliation, had offered eggs for sale in the Australian Capital Territory, Bartters major market, at some ten cents lower than the price charged by it in Victoria. The Full Court found that the Board had offered the eggs at that price with the intent of harming Packwood and granted an injunction against the Board.

In **Trade Practices Commission v. C.S.B.P. & Farmers Ltd**\(^{35}\), the defendant was a sole distributor of urea in Western Australia. It obtained this fertiliser from Consolidated Fertilizers Ltd (C.F.L.), a firm located in the Eastern States. Prior to the commencement of the Trade Practices Act, it was the sole distributor of urea in the western State. This exclusive dealing contract was abandoned with the introduction of the Act. However, even after that a farmers cooperative, Rural Traders' Cooperative (R.T.C.) had been refused a distributorship of urea by C.F.L. Consequently R.T.C. entered into negotiations to import urea from Italy, to be sold in the Australian market from 17th October 1975 at $145.00 per tonne, considerably lower than the price charged by C.S.B.P. of $178.70 per tonne. R.T.C. also contacted C.F.L. in late September to see if it was prepared to match that offer, C.F.L. replying that it intended to maintain distribution through C.S.B.P. On the day prior to R.T.C.'s commencement of sales, C.S.B.P. announced a reduction of its price to $144.60, undercutting the R.T.C. price by


$0.40.

The case against C.S.B.P. failed because there was no clear evidence that C.S.B.P. lowered its prices for the purpose of harming its competitor R.T.C. According to Fisher J. although the announcement of the new price by C.S.B.P. may have been to an extent accelerated, there was nothing in the fixation of the new price at that time and at that figure which would justify a finding of predatory conduct\textsuperscript{36}.

(d) Evaluation of S. 46. Section 46 is very suited to curb primary line abuse because it incorporates price discrimination within the provisions of monopoly control.

(i) It begins by excluding from its jurisdiction those firms that do not have market power. Thus firms not in a dominant market position are given a sanctity when pricing which is not given them under the Robinson-Patman Act. This diminishes the anti-competitive aspects of anti-price discrimination law and reduces pricing inflexibility. It allows small firms and new entrants to embark on pricing policies (such as promotional pricing) without fear of prosecution under the section.

(ii) The purpose test serves to distinguish those acts embarked upon for a genuine pro-competitive reason from those undertaken to destroy a competitor. The effect of this is to move the emphasis of the section away from the competitive injury test and towards the 'dominant market position' and 'purpose' tests. As a consequence, the competitive injury test can be worded so as to protect an individual competitor. When the market is already dominated by a single firm and that firm actively intends to destroy its competitors, the protection of competitors is a more desirable test than the protection of competition.

(iii) Section 46 does not contain the added jurisdictional requirement of discriminatory pricing.

\textsuperscript{36} [1980] ATPR 40-151 at 42,166.
(iv) Section 46 applies to both goods and services.

Thus Griffen writes\(^{37}\):

I doubt...whether section 49 adds anything to the provisions of section 46 where the issue is seller-line injury. Indeed, in view of the wider ambit of the anti-competitive test of section 46, some discriminatory conduct will not be caught by section 49 but will fall within section 46. In view of the complexities of section 49, it may well have been better for the seller-line injury to have been left exclusively in the province of section 46.

However, the reluctance of the Courts to infer intent from the circumstances of the price reduction suggests that the purpose requirement may substantially limit the application of the section. The C.S.B.P case can be contrasted with the Packwood case where predatory intent was inferred from the surrounding evidence, however, these cases do show that if the section is to be given proper effect a Court must be prepared to find predatory intent even in cases where there is no direct evidence of such intent, (especially as there rarely is any direct evidence in predation cases). The presumption that a person intends the natural consequences of his actions (i.e. the elimination of a competitor) can be used to infer predatory intent.

A second limitation of this section to control price discrimination is that it is ineffective in secondary line cases. Although a large buyer may be in a position to substantially control a market and may abuse that position to gain discounts, the firm will not usually be motivated by a desire to exclude a competitor or erect barriers to entry but by a desire to gain a competitive advantage. Thus no predatory intent exists. Of course, the section was not designed to capture secondary line cases, but this does mean that if Section 49 were repealed, only its primary line proscriptions could be transferred to Section 46 and a policy towards secondary line injury would have to be

\(^{37}\) Griffen, \textit{op. cit.}, p. 46.
developed separately.

(2) Discrimination to Enforce Resale Price Maintenance and Exclusive Dealing

Both the exclusive dealing and the resale price maintenance provisions of the Act contain clauses preventing the use of discriminatory pricing to enforce an otherwise illegal contract.

Under Section 96(3) (d) & (e), withholding the supply of goods for the purpose of enforcing RPM is condemned. Withholding supply is defined in Section 98(1):

98 (1) For the purposes of paragraph 96(3) (d) or (e), the supplier shall be deemed to withhold the supply of goods to another person if -

(a) the supplier refuses or fails to supply those goods to, or as requested by, the other person;
(b) the supplier refuses to supply those goods except on terms that are disadvantageous to the other person;
(c) in supplying the goods to the other person, the supplier treats that person less favourably, whether in respect of time, method or place of delivery or otherwise, than the supplier treats other persons to whom the supplier supplies the same or similar goods; or
(d) the supplier causes or procures a person to withhold the supply of goods to the other person as mentioned in paragraph (a), (b), or (c) of this sub-section.

Section 98(2) contains certain exceptions if the the buyer uses or has used the goods as loss leaders.

The section forbids the 'hold-them-in-line' type of discrimination. As such, the discrimination is ancillary to the main offence, which is the resale price maintenance or the exclusive dealing.

However, although the competitive impact of the discrimination is not important, the meaning of 'discrimination' is.

Section S. 98(1)c contains a simple test of discrimination. Its salient features are that it is limited to conditions of delivery, it does not distinguish between buyers who are not in competition with each
other (ie. buyers who may be in a different geographic, product or functional market), and it contains no defences to justify the discrimination (such as cost justification) although these defences may be implicit in the Act.

The 'disadvantageous' test in S. 98(1)b at first glance requires no comparison between purchasers. However, Donald and Heydon write:\textsuperscript{38}:

"Disadvantageous" connotes relativity. Reference should be made to the general terms of supply prevailing with respect to the same or like kind of goods....The paragraph does not indicate whether the disadvantage suffered by the other person is to be measured by reference to the terms usually granted to that person alone or by reference to the terms granted to other persons in similar circumstances or to other persons generally. It seems desirable that the court should adopt the approach of a commonsense business person to the issue. If a supplier has been supplying goods to a retailer for some time, it would be easier to determine whether a change in the terms of supply would place the retailer in a less advantageous position. However, in the case of a first supply of goods to a retailer, there would exist no prior terms of supply to provide a yardstick by which to judge whether terms are "disadvantageous"; the position of the retailer would have to be compared with other retailers. Where a wide range of retailers is available, the comparison will be with those in positions most nearly resembling the subject retailer, account being taken of relevant dissimilarities....The disadvantage (if any) is not to be judged by its actual effect on the person to be supplied but on its likely effect. The test is objective and involves a determination based upon the discriminatory terms themselves. An actual disadvantage sustained may assist in this determination.

Although neither test contains any defences, if the seller can show that the terms granted to a buyer differed because of cost-savings, changing conditions or differing competitive pressures from other sellers, the Court may be convinced that the reason for the discriminatory terms was not to enforce RPM but for another legitimate trade purpose. Thus these defences are implicit in the section.

The use of the term "disadvantageous" has both advantages and disadvantages. It is undefined and vague and therefore may be used in a

\textsuperscript{38} Donald and Heydon, \textit{op. cit.}, pp. 375-376.
flexible manner to catch anti-competitive behaviour. However, its vagueness also gives rise to uncertainty in the courts and among the business community. For example, it is not clear, when inter-firm comparison is made, if the two firms need be on the same functional level.

Section 47(3) and (7) prohibit the granting of discriminatory terms. Both sections read:

A corporation also engages in the practice of exclusive dealing if the corporation refuses-
(a) to supply goods or services to a person;
(b) to supply goods or services to a person at a particular price; or
(c) to give or allow a discount, allowance, rebate or credit in relation to the supply or proposed supply of goods or services to a person....
for the purposes of enforcing an exclusive dealing agreement.

(3) Contracts, Agreements, or Understandings in Restraint of Trade

Where discriminatory terms are granted to some buyers, it is possible to interprete the sales contracts made by the seller and the favoured buyers as contracts with the purpose, effect or likely effect of substantially lessening competition. There may be special advantages in bringing a case under this section as all contracts entered into by the offending parties may be aggregated for the purpose of determining competitive impact. This is especially relevant in secondary-line cases where a large buyer receives discriminatory discounts from a number of different sellers. This section may also provide a means to attack industry-wide pricing agreements such as delivered pricing agreements. The difficulty with the use of this section is it may not extend to parallel business behaviour, or to contracts or agreements where there is another credible explanation for the behaviour.

(4) The Petroleum Retail Marketing Franchise Act 1980

Following allegations of price discrimination in the petroleum industry the Petroleum Retail Marketing Franchise Bill was enacted in 1980. Its strong provisions are intended to discourage any price discrimination in the industry. For this reason it contains no competitive injury clause and price discrimination is per se illegal. Its main provision relating to price discrimination reads:

20 (1) A franchisor shall not, in relation to motor fuel supplied or to be supplied by it, discriminate between its franchisees in relation to-
(a) the amounts payable by the franchisees in respect of the fuel; or
(b) any discounts, allowances, rebates or credits given or allowed to the franchisees in respect of the fuel.

(2) Subsection (1) does not apply in relation to a discrimination if-
(a) the discrimination makes only reasonable allowance for differences in the cost or likely cost of raw materials, refining, distribution, sale or delivery resulting from the differing places to which methods by which or quantities in which the motor fuel is supplied to the franchises;
(b) the discrimination is constituted by the doing of an act in good faith—
(i) to meet a price or benefit offered by a competitor of a franchisor; or
(ii) to assist a franchisee to meet a price or benefit offered by a competitor of the franchisee.

5.3 CONCLUSIONS

Section 49 has not proved successful from the view of supporters or opponents of price discrimination law. A selected review of some submissions to the Blunt Committee reflect the opposing views:

Australian Chamber of Commerce:\(^{40}\):

Section 49 is having an adverse effect on competition in industry, in that instead of promoting competition, it is actually inhibiting price movements. Some firms have used

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\(^{40}\) Blunt Committee Report, Vol. II, p. 149.
this Section to reduce the discounts offered to distributors and retailers, and have hidden behind the Act to do so.

Dept. of Industry and Commerce:\(^\text{41}\);

3.5.9...although S49 in our view is of little value to an individual small business suffering from price discrimination, it appears to have some deterrent effect on this practice, particularly as businessmen realize there is a difference between genuine discounting and blatant price discrimination.

The Retail Traders' Association of N.S.W.:\(^\text{42}\):

...we have had complaints about alleged ability of larger retailers to sell at lower prices, but few have seen that Section 49 is relevant. The answer in practice in almost every case is provided by the formulation of buying groups which have become remarkably effective in equalizing buying terms. On occasions it has been put that Section 49 is unnecessary and that the monopolisation provisions under Section 46 contain the crucial power inherent in ensuring a continuation of the competitive scene.

Council of Small Business Organisations Of Australia:\(^\text{43}\):

COSBOA has consistently stated that, whilst it strongly supported the retention of section 49 of the Trade Practices Act, it was felt that the wording of the section left much to be desired. We suggest therefore that consideration should be given to a redrafting of the Section.

(a) Primary Line Injury. Section 49 of the Trade Practices Act may be compared with Section 46 as a means of controlling price discrimination causing primary line injury. Because it is not the discrimination but the low predatory price that causes the injury, Section 46 is better suited to primary line injury cases. Its provisions focus on the size of the predator and it is concerned with injury to competitors in a concentrated market. Section 49 has an additional and unnecessary jurisdiction element of establishing a price discrimination.

(b) Secondary Line Injury. The criticism of Section 49 is

\(^{41}\) ibid, p. 285.

\(^{42}\) ibid, p. 428.

\(^{43}\) ibid, p. 239.
centred on the competitive injury clause. The test requires the discrimination to be recurring or systematic in nature, and for the effect of the discrimination to injure competition. The first test is better suited to secondary line cases because, as was shown by Morton Salt, only such a low standard is suitable for secondary-line cases.

The second test is used to avoid the anti-competitive consequences similar to those caused by the Robinson-Patman Act. However, this test requires a higher standard of injury, something that is usually not present in secondary line cases, making the section unsuited to deal with typical secondary-line cases such as Morton Salt.

Although the standard of competitive injury required to establish a secondary line violation is unclear, with Franki J. and Sheppard J. taking opposing views in the Cool v. O'Brien case, the wording used in Section 49 suggests that there was no intention to incorporate the incipiency doctrine into the Section. Thus the threshold of competitive injury would have to be lowered if the section is to achieve its purpose of controlling secondary line injury.

(c) The Future of Section 49. The decision to retain, amend, or repeal Section 49 has been political rather than logical. There are many small business interests lobbying for the retention and strengthening of the Section. To this point their lobbying has been successful and it seems certain that Section 49 will be retained. The small business is an important sector that no politician can afford to

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44 Eg. Comments of Ron Bannerman, Chairman of the Trade Practices Commission, "I think we all should acknowledge that decisions are not going to be made about amendment of section 49 simply on economic grounds. No government, this or any other, would limit itself to that."..."The matter is clearly one for political judgement by the Government and Parliament", The Trade Practices Commission's View of the Proposed Amendments, a paper given as part of a seminar entitled The Proposed Trade Practices Amendments: Their Legal and Economic Impact, conducted by the Business Law Education Centre, Sydney 22 March 1984, Melbourne, 23 March 1984, p. 69. See also Pengilley, Handbook on Price Discrimination: The Present Position and the Impact of Legislative Proposals, p. 76.
ignore.

However, we conclude that Section 49, a modified form of the Robinson-Patman Act, has not had a beneficial impact on the Australian economy. Two problems are obvious: the Australian legislations have failed to recognise that price discrimination causing primary line injury is best dealt with under the monopolisation provisions and they have failed to recognise the inconsistency between a high standard of competitive injury and the need to provide adequate protection against secondary line injury.

Amending the section by lowering the competitive injury test will not be successful. There is nothing distinctive about the Australian economy that suggests that an amended section is likely to have fewer or less serious anti-competitive effects than the Robinson-Patman Act. In fact, the higher level of concentration and the greater competition caused by imports suggests that anti-price discrimination legislation is likely to have a more deleterious impact on the economy.

The recommendations of the Blunt Committee are therefore accepted. The strengthening of the Section is rejected. Indeed, the pro-competition and pro-efficiency objectives of the Act are best served by the repeal of S. 49. Section 46 should give adequate protection to small businesses from the predatory tactics of their larger rivals.
CHAPTER VI

A COMPARATIVE STUDY OF PRICE DISCRIMINATION LAW

The United States and Australian approach has not been completely successful in identifying and eliminating anti-competitive price discrimination. Other developed countries have also legislated against price discrimination. A review of the legislation in these countries may reveal a variety of approaches, some with particular merits.

6.1 COMPETITION LAW IN THE EEC

(1) The Treaty of Rome

The law pertaining to price discrimination in the EEC can be found in two sections of the Treaty of Rome, which governs competition within the EEC. Section 85 covers agreements likely to affect trade between member countries, while section 86 prevents abuse of power by a firm in a dominant position. Both sections provide examples of, (but are not restricted to), the type of practice which may animate the Treaty provisions:

85(1) The following shall be deemed to be inconsistent with the common market and shall be prohibited, namely: all agreements between firms, all decisions by associations of firms and all concerted practices likely to affect trade between the Member States and which have the object or effect of preventing, restraining or distorting competition within the common market, and in particular those which:

... (d) apply dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

86 Any abuse by one or more undertakings of a dominant position within the common market or in a substantial part of it shall be prohibited as incompatible with the common market insofar as it may affect trade between
Member States. Such abuse may, in particular, consist in:

(c) applying dissimilar conditions to equivalent transactions with other trading parties, thereby placing them at a competitive disadvantage;

Caution must be taken when interpreting these sections. In particular, it must be considered that the objective of competition law in the EEC differs from the U.S. objective. Indeed, the common theme found in cases decided by the Court is the willingness to employ the Treaty to break down trade barriers that separate Member States. To achieve this objective there has been scant regard for the precise letter of the law, which can be seen as grossly inadequate to prevent anti-competitive price discrimination.

(2) **Article 85(1)**

An early case decided under the Act was in **Re Kodak**. Kodak applied for a negative clearance for a trade practice that forced all buyers of Kodak equipment to pay the Kodak subsidiary that operated in the country of the buyer at prices determined by that subsidiary. The consequence of this trade practice was to force a buyer to purchase Kodak equipment locally because he could no longer receive the cheaper prices offered by a foreign company. This had the effect of preventing price arbitrage between the member countries. Price discrimination occurred because the local Kodak subsidiary would supply identical goods to local and foreign purchasers at different prices.

When refusing to grant clearance, the Commission first had to

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1 Consider the prohibitions of Articles 85(1) and 86, and also Article 7 which has a pervasive influence on the interpretation of the Treaty:

(7) **Within the field of application of this Treaty, and without prejudice to any particular provisions mentioned therein, any discrimination on the grounds of nationality shall be prohibited.**

2 In **re Kodak**, CCH, Common Market Reporter P9378.
surmount the hurdle of finding an 'agreement' between firms. The Commission found this, but not in the agreements between the parent Eastman-Kodak and its subsidiaries, nor between the subsidiaries themselves, but between the subsidiaries and their buyers. This interpretation of 'agreement' seems to contravene the spirit of Article 85(1) which seems to be aimed at horizontal agreements\(^4\).

The second area of confusion was whether the agreement caused competitive injury. As buyers in the high and low priced countries were not in competition, it was uncertain how the agreement could affect competition between them as required by the section. Although the Commission did not specifically mention Article 85(1)d, they did refer to the competition element\(^5\):

The sales conditions had the effect of isolating the markets of each member state and of excluding from competition in one or more member states the prices charged in each of these markets. Hence, these conditions restricted competition within the Common Market and were capable of affecting trade between member states.

Some writers prefer to see this case as an attack on unilateral action which prevents trade between member-states\(^6\), whereas others see

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\(^3\) Under regulation 17/62, Article 2, the Commission may find according to the information it has obtained, that there is no grounds for it, under Article 85(1) or Article 86 of the Treaty of Rome to intervene against an agreement, decision or concerted practice. Such a decision is called a negative clearance.


\(^5\) Para. 17 of the Decision.

\(^6\) Canenbley op cit; Scheuermann op cit.
it as an extension of the Treaty to cases of unilateral price discrimination.  

(3) Article 86

Article 86 contains a strange deficiency. Although concerned with the abuse of a dominant position, it requires injury to competition at the secondary level. In Hoffman-La Roche v. Commission, Roche was found to have a dominant position in many of the product markets in which it sold, each vitamin group being treated as a separate market. Roche used a volume discount system linked to an exclusive dealing contract. If a buyer brought all or most of its supplies from Roche, the volume discount was granted.

Injury was found at the primary level because of the foreclosure effects of the 'fidelity' discount, and at the secondary level because of the disparate treatment of buyers. The foreclosure effect may be analysed in two parts. First, the fidelity discounts bind buyers to Roche, and second, because the discounts were granted on overall purchases of all groups of vitamins, equally efficient firms could not offer comparable discounts unless they produced an entire range of vitamins and this represented a barrier to entry.

Also of interest is the so-called 'english' clause, which allows a buyer to inform Roche of better competitive offers and, if Roche did not respond with similar offers, the buyer could purchase from the competitor without endangering his fidelity discount. This clause was interpreted as allowing Roche to identify strong competitors and eliminate them by continually matching their prices. This reinforced the

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7 Eg. Lazerow op. cit.

primary-line effects of foreclosure.

As vitamins formed a very small percentage of input of the final product, the relatively small rebate could have negligible effect on secondary-line competition. Nevertheless the Court gave weight to the importance that buyers placed on such discounts and found secondary line injury has been impaired. Zanon writes "it seems that the Courts are only paying lip-service to one of the requirements imposed by Article 86", and, after noting the similarity between this and the *Morton Salt* decision, he continues:

[T]he similarity of the EEC Commission and the [Supreme] Court's approach reveals once more that the basic goal of European anti-trust is to protect the expansion of the small at the expense of the large, rather than to foster the expansion of the efficient at the expense of the inefficient.

Another controversial case is *United Brands Co. and United Brands Continental B.V. v. Commission* 10. Here the price discrimination was not employed to foreclose the market to competitors, but to maximise the profits of the seller. United shipped its branded Chiquita bananas from Central America. (The level of supply to the European market was therefore fixed). Three to four days prior to the berthing of the ship, United set the price and quota of bananas to each buyer. This price and quota was based on the profit potential of each national market and not the costs of transporting the goods from Central America. These buyers held the bananas until ripe and then resold them to retailers. During the time when the bananas were stored, the buyers were forbidden to resell them to other buyers. By way of this 'Green Banana Clause', United prevented arbitrage between national markets. (After the goods were ripened, it was not possible to transport them a long distance and

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9 Zanon, *op. cit.*, p. 319

therefore there could be no arbitrage at this time).

The policies allowed United to separate markets and thereby extract maximum profits from each country. The Courts objected to this for two reasons. First, the imposition of the 'Green Banana Clause' partitioned the Common Market, and this was an abuse of a dominant position. This abuse harmed secondary line competition as it had the effect of creating "price levels which were artificially different, placing certain distributor/ripeners at a competitive disadvantage, since compared with what it should have been, competition had thereby been distorted"\(^1\).

The second criticism was that United should have related prices to costs rather then charging what the market would bear. The Court reasoned this because it was the buyers and not United who bore the risks of the market, as United was too far removed from the distribution level where the supply and demand forces interacted. This reasoning is tenuous. First, United set quantity levels well before demand could be determined and therefore it did bear some of the risks. Second, the forces of demand and supply function at all levels of distribution and cannot be confined merely to the retail level.

The main objection to United's policies may be considered to be the 'Green Banana Clause' preventing free trade between EEC states, although this was not prominent in the Court's decision. Alternatively, the existence of a profit-maximising price discrimination may have been the deciding factor. However, to eliminate the 'Green Banana Clause' might encourage United to cease supply to low-price countries such as Eire, and maximise profits by supplying only to high price countries.

The significance of the United Brands case is not clear. This case and Kodak suggests that the primary purpose of the EEC anti-price

\(^1\) 1 CMLR 429, 500-501 (1978).
discrimination rules is to break down trade barriers and not to attack the predator or the big buyer. The price discrimination provisions, although in many ways inadequate, have been interpreted broadly to allow the Court to achieve this objective.

(3) The Treaty of Paris

The Treaty of Paris, which establishes the European Coal and Steel Community, contains a third piece of anti-price discrimination legislation. Article 60, Section 1, Clause 1 prohibits "practices of unfair competition, in particular, price cuts of a merely temporary or local nature, aimed at the achievement of a monopoly in the Common Market", while Clause 2 prevents unequal terms being applied to comparable sales, and specifically where the discrimination is based on national identity. Section 2 assigns to the High Authority the task of prescribing the extent and form in which producers must publish their price lists. Basing-point pricing is accepted, although the High Authority may proscribe the use of unusual basing points. A seller may also 'align' (or meet) the prices of competitors so long as the competitor's price is not undercut.

In Decree No. 30/53, the High Authority prohibited all deviations from published price lists, however, subsequently it has accepted variations arising from -

(i) transactions that are not of a comparable nature,
(ii) deviations that are granted equally to all buyers,
(iii) the legitimate 'alignment' of prices.

A seller may grant functional discounts and loyalty rebates to buyers on the ground that these represent non-comparable transactions. These discounts need not be cost-justified, although they must be shown in the price lists and they must be available to all buyers who qualify for them.
In general, Article 60 has the objective of obtaining 'fair competition', achieved through the price notification system and an 'orderly' open price system. The Article does not require a showing of competitive injury and this enhances its anti-competitive impact. It enshrines the basing-point system with a legality which it did not have prior to the Treaty and is directed to achieving an orderly code of marketing conduct.\(^{12}\)

6.2 THE UNITED KINGDOM

There is no law directly prohibiting price discrimination in the United Kingdom, despite the phelora of statutes controlling undesirable restrictive trade agreements and monopolistic practices.\(^{13}\)

(1) The Resale Prices Act 1976

Nevertheless there are two contexts where price discrimination may be considered. The first is the case where price discrimination is used to force compliance with a RPM agreement. Here, price discrimination is a variant of refusal to supply and the questions of public interest (including competitive injury) are formulated in terms of the RPM agreement and not the discriminatory pricing. These provisions are contained in the Resale Prices Act 1976.

Under the Fair Trading Act 1973, the Director of Fair Trading, the Secretary of State for Prices and Consumer Protection, or the other Ministers may refer to the Monopolies and Restrictive Practices


Commission "any preference given to any person (whether by way of discrimination in respect of prices or in respect of priority of supply or otherwise) in relation to the supply of goods or services"14. Following a Report by the Commission that the practice operates to the detriment of the public interest15, the appropriate Minister may issue one of the Orders listed in Schedule 8 of the Fair Trading Act 1973. One such Order, Paragraph 6, reads:

(6) An order may declare it to be unlawful, except to such extent and in such circumstances as may be provided by or under the order —
   a) to discriminate in any manner specified or described in the order between any persons in the prices charged for goods or services so specified or described, or
   b) to do anything so specified or described which appears to the appropriate Minister to amount to such discrimination,
   or to procure others to do any of the things mentioned in sub-paragraph (a) or sub-paragraph (b) of this paragraph.

A major purpose of the Competition Act 1980 was to speed up this process of investigation, report and order. The Director General is authorised to investigate a practice and, where appropriate, accept an undertaking from the firm concerned, failing which he could refer the firm and the practice to the Monopolies Commission.

The Commission has indicated in a number of cases the circumstances where discriminatory pricing may be contrary to the public interest. In the Contraceptive Sheaths reference16, the Commission objected to the use of discriminatory pricing to prevent new entry to the market; in Frozen Foodstuffs17, the Commission objected to the use of monopoly profits gained in one product line to sustain a loss operation in another product line. And in two references, Electrical

14 Paragraph 49(3)d.
17 [1976] HC. 674 paras. 337.
Equipment for Vehicles\textsuperscript{18} and Clutch Mechanisms for Road Vehicles\textsuperscript{19}, the disparity between initial and replacement parts caused by monopsonic power of large automotive assemblers was the cause of concern.

However, these Reports may be compared with those of Rank Xerox\textsuperscript{20}, where the discrimination allowed penetration into new markets, Frozen Foodstuffs\textsuperscript{21} where the lower price available for larger packs of the product encouraged more efficient methods of distribution, and Footwear Machinery\textsuperscript{22} where the Commission noted it did not expect constant cost/profit ratios.

The United Kingdom approach has been to treat price discrimination largely within the structure of monopoly control. This has resulted partially from the traditional concern of British antitrust for the welfare of the public and a disregard for the position of the individual trader (except where the two concerns are synonymous). Thus, issues of fairness are not given the same weight as in countries such as the United States or Eire\textsuperscript{23} and therefore there has not been the same motivating force for specific legislation.

Another factor contributing to the lack of regulation is the findings of the Monopolies and Mergers Commission resulting from a study of the food retailing industry\textsuperscript{24}. Prior to this, the Commission had condemned five principal types of price discrimination:

\textsuperscript{18} [1963] HC. 21.
\textsuperscript{19} [1968] HC. 32.
\textsuperscript{20} [1976] HC. 47 paras. 403.
\textsuperscript{21} [1976] HC. 674 para. 335.
\textsuperscript{22} [1973] HC. 215 paras. 205-254.
(i) loyalty rebates, paid to retailers who refrain from dealing with other retailers,

(ii) requirements rebates, calculated on the proportion of the purchaser's volume satisfied by the seller,

(iii) aggregated rebates, calculated on the total purchases of all product lines from a single seller,

(iv) rebates for promotional services, paid to retailers who devote a given proportion of their display facilities to the supplier's products,

(v) retrospective rebates, payable only after a new supply contract subsequent to the one on which the rebate has been earned has been entered into\(^{25}\).

The common theme with these rebates is they are granted by the seller to secure the loyalty of the buyer and therefore they have a foreclosure effect on other sellers.

The Commission found that the industry structure had changed and that now discounts usually resulted from the pressure of buyers rather than the monopolistic aims of the sellers. The Commission concluded that this new situation was not necessarily contrary to the public interest. Increased efficiency had the effect of maintaining the profit levels of sellers while vigorous rivalry between chains ensured that prices at the retail level were maintained at a competitive level. (Although the greater concentration found at the retail level did increase the possibility that an oligopolistic pricing structure could occur). The Commission also conducted a survey which indicated that fewer than half the manufacturers and almost no distributors attempted to cost-justify their discount structures and this finding seemed to

preclude resort to a price discrimination statute incorporating the cost-plus concept.\(^{26}\)

Price discrimination is seen as a problem of concentration, both at the seller's and the buyer's level. Greater reliance has been placed on anti-monopoly and anti-merger provisions to limit the growth of monopoly power than specific legislation to the control of abuse of power once it has been created. Thus, a specific price discrimination statute may be seen as inconsistent with the basic approach to the problem of monopoly in the United Kingdom.

6.3 EIRE

(1) The Irish Framework of Control

The Irish approach to restrictive trade practices is significantly different from that which prevails in most other western countries and it is through this alternative framework that price discrimination is controlled.

The law relating to competition is contained in the Restrictive Trade Practices Act 1972, which originated from the Restrictive Trade Practices Act 1953 (and the Restrictive Trade Practices Amendment Act 1959). The earlier Act established the Fair Trade Commission, a body with two distinct functions. The first was to promulgate Fair Trade Rules to govern conditions of supply and distribution of specified goods. These rules had no legal backing until the Minister for Industry and Commerce, upon receipt of a Report from the Fair Trade Commission, issued an Order affirmed by Parliament. The second function of the Commission was to hold enquiries into the conditions of supply and

\(^{26}\) See generally Meekin, op. cit.
distribution of specified goods\textsuperscript{27} and, upon completion of the enquiry, to report to the Minister for Industry and Commerce describing the conditions existing, their impact on competition, and whether the effects were unfair or contrary to the public interest. The Minister could then make an order controlling particular trade practices which, upon being affirmed by Parliament, had the force of law. The 1972 Act did not significantly alter these functions or procedures, except that the post of Examiner of Restrictive Practices was established. A practice was (and still is) evaluated according to a standard of fairness and a standard of competition\textsuperscript{28}

(2) Application of the Act to the Grocery Retailing

A representative application of this law to price discrimination occurred in the grocery industry\textsuperscript{29}.

15(1) A supplier or wholesaler shall not, as respects the terms and conditions on which goods (of like grade, quality or quantity) to which this Order applies may be obtained from him, differentiate by means of any rebate, refund, discount, credit or any other similar concession or by the provision of any service, facility or other consideration of value, between one purchaser for resale and another purchaser for resale (being purchasers of the same class).

(2) Paragraph (1) of this Article shall not apply to differentiation based on \textit{bona fide} considerations of creditworthiness by the supplier or wholesaler as to the time within which payment is to be made to him for goods supplied.

The Order had the weakness of requiring comparable sales to be of similar quantity, and it prohibited discrimination only between members

\textsuperscript{27} The Commission may initiate an Enquiry only after investigation by the Examiner of Restrictive Practices, a position established by the 1972 Act. Formerly, the Commission could commence an Enquiry on its own motion, or on the motion of the Minister of Industry and Commerce, or any other interested person. The purpose of the new position of Examiner of Restrictive Practices was to separate the functions of investigation and adjudication.

\textsuperscript{28} Section 3 and Third Schedule.

\textsuperscript{29} Restrictive Trade Practices (Groceries) Order 1956.
of the same class.

The Order was primarily concerned with Resale Price Maintenance, restricted entry, price fixing, etc, and was found inadequate to deal with the problems arising from the growing concentration and vertical integration that occurred in the late 1960's. Large supermarkets pressed for advantageous terms, with the result that suppliers produced two price lists, one called 'Standard Terms', the other 'Supplementary Terms' - the latter prices being lower and made available only to multiple-outlet supermarkets. In addition, suppliers would make 'split drops', that is, deliver small quantities of goods to each outlet of a multiple-outlet supermarket at favourable prices. Wholesalers found themselves disadvantaged as they brought at similar terms yet had to perform this distribution function themselves.

Following a Report by the Commission\(^\text{30}\), which emphasized fairness more than competitive impact, the Minister made an Order, The Restrictive Practices - (Groceries) - Order, 1973, which sought to eliminate the discriminatory terms prevailing in the industry:

3(1) (a) A supplier shall prepare and maintain a statement in writing containing the terms and conditions upon and subject to which he sells grocery goods (including supplementary terms, if any, and, if he grants credit in respect of the purchase price of any grocery goods, the terms and conditions of such grant), and the supplier shall effect a sale of grocery goods of any kind to wholesalers or retailers upon and subject to those terms and conditions (in so far as they apply in relation to that sale of that kind of goods).

3(2) The terms and conditions aforesaid may make provision for discounts of different amounts on the prices of goods sold related to

(a) the different functions in relation to sale and distribution of the goods performed by purchasers of the goods, or

(b) the quantity or value of goods,...

A person may make provision for different functions performed by purchasers or different quantities or values in which they buy if these differences are cost justified.

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Implementation of the Order was difficult as theory became divorced from practice. The reasons for this failure are summarised:\(^{31}\):

First, manufacturers have been afraid to prepare and publish statements of terms, because the differences they would exhibit between wholesaler customers and multiple retailer customers would result in their being unduly pressurised. Secondly, should the manufacturer have had the courage to publish new terms as required, the multiples thereupon refuse to stock his goods, and so, to ensure the continuation of business, he reverts to his old terms. Thirdly, if a manufacturer's new terms are not operated, the wholesale group who would derive the benefit from them threaten to take their own action. And fourthly (and finally), the interpretation of parts of the Order are hotly contested.

This resulted in the Amendment Order 1978 which relaxed the prohibition against discriminatory terms but did not clarify the law. Because of exacting standards of evidence, few prosecutions have proceeded and the main form of enforcement is by negotiation, persuasion and pressure by the Fair Trade Commission and, since 1972, by the Examiner.

(3) Conclusion

The Irish Orders have combined the prevention of unfairness with the need for flexibility. Although the Irish approach to competition law is interesting, it has failed to curb undesirable price discrimination. This failure results from the inadequate wording of the Orders and the lack of strong enforcement.

The approach does have the feature that it allows competition laws to be limited to concentrated industries whereas the Robinson-Patman approach limits all price discrimination. However, it is precisely those concentrated industries where price discrimination is likely to have its greatest pro-competitive effect:\(^{32}\). Unlike mergers, which almost always aggravate a concentration problem, the same cannot

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\(^{31}\) Ann R. Everton, op. cit., p. 37.

\(^{32}\) See the comments of Breyer, supra, p. 278.
be said for price discrimination, and thus it may be undesirable to
apply the law only to specific areas. Another problem with the Irish
approach is the danger that, as Parliament is the final decision-making
body, the process of making an Order may become a matter of politics and
lobbying power rather than competition policy.

6.4 CANADA

(1) Control of Price Discrimination in Canada

Anti-price discrimination legislation was originally introduced
into Canada in 1935 (prior to the enactment of the Robinson-Patman Act)
by Section 498A of the Criminal Code. Similar to the Robinson-Patman
Act, its introduction reflected concern with the abuse of monopsonic
buying power and the need to protect small enterprises and the consumer
from the potential abuse that could arise from industrial
concentration 33. Its provisions sought to prohibit such unfair and
oppressive practices as "discriminatory discounts, rebates and
allowances, territorial price discrimination, and predatory price
cutting" 34. The provisions remained substantially intact through several
minor amendments to become Section 34 of the Combines Investigation Act.

34(1) Anyone engaged in a business who —

(a) is a party to, or assists in, any sale that
discriminated to his knowledge, directly or
indirectly, against competitors of a purchaser of
articles from him in that any discount, rebate,
allowance, price concession or other advantage
that, at the time the articles are sold to such
purchaser, is available to such competitors in
respect of a sale of articles of like quality and
quantity;...

is guilty of an indictable offence and is liable to
imprisonment for two years.

The Section has several distinctive features which deserve

33 Eg. See Royal Commission on Price Spreads, Report, 1936.

34 ibid, p. 8.
highlighting. Subsection 34(1)a outlaws price discrimination with secondary line effects although it does not require a showing of competitive injury. Rather, to create liability, the seller must grant the concessions "as part of a practice" of discrimination. In this way, it is similar to the 'systematic' requirement of the Australian Trade Practices Act 1974 and the proposals of the Neal Committee, however, 34(1)a does not extend to the singular, large, anti-competitive discount. The section also requires a discrimination between sales of goods "of like quality and quantity" and this provides a loop-hole, identical to that which existed in the original Clayton Act 1914, for the seller who discriminates between buyers who purchase in different quantities. Notable omissions from the provision are any reference to buyer liability and to the cost justification defence for different methods of purchasing.

Subsection 34(1)b prescribes territorial price discriminations which have the "effect or tendency of substantially lessening competition or eliminating a competitor...or designed to have such effect". The competitive injury test therefore can be seen as very broad.

Subsection 34(1)c deals with the selling of products at prices that are "unreasonably low". The broad competitive injury test used in 34(1)b is repeated here. Finally both 34(1) (b) and (c) require that the seller engage in a "policy" of such proscribed conduct, thus limiting the application of the Act to systematic rather than incidental pricing.

Although the definition of 'price' in Section 34 is very expansive, Section 35 contains a separate prohibition against the granting of promotional allowances except on proportionate terms to all

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35 This requirement now contained in Section 34(2) was introduced in the 1952 Amendment. This requirement also seems to allow a 'meeting competition' defence where the seller meets the spot prices of a competitor.
buyers. This provision was adopted in 1960 in response to a specific problem of sellers circumventing the legislation by offering promotional allowances.

A feature distinguishing the Canadian anti-price discrimination legislation and the Robinson-Patman Act is that the former are criminal provisions whilst the latter is civil, and there is a knowledge requirement for both primary and secondary line offences.

(2) Evaluation of the Canadian Law and Proposed Amendments

Few cases have been decided under the sections. It is suggested that this is because of the inadequacy of an Act which allows discounts to buyers of different quantities and requires a higher standard of proof because of its criminal nature. These represent significant drawbacks of the Canadian approach.36

Recently there have been proposals to amend the Act. These proposals have culminated in Bill C-13. The proposed amendments expand the law in two areas.

A Competition Board would be established with power to prohibit "unfair" price discrimination (ie. price differentials that do not correspond to cost savings) by a major supplier in an industry where price discrimination is prevalent if the discrimination has the effect of impeding substantially the growth of an efficient firm or a potentially strong competitor.

Second, criminal provisions attacking delivered pricing would be established. Under these provisions, a supplier may be ordered not to refuse one of his customers the opportunity to take delivery of an article at any location at which the supplier makes delivery to any other of his customers on the same terms and conditions that would be available if the customer's place of business was in that locality. The

36 Ann Everton, op. cit., p. 25.
section only applies when the practice is engaged in by a major supplier or is widespread in the industry, and the customer is denied an advantage that could otherwise be available to him. In effect, an existing customer can obtain the same terms as any of the suppliers other buyers.

These provisions are not meant to eliminate all delivered pricing. They express a concern for the problems that delivered pricing may cause. In particular, the danger of increased collusion, the distorting effect that delivered pricing systems have on buyer’s location, and the possibility of excessive cross-hauling\textsuperscript{37}. Indeed, they are of very limited application and could not achieve the purpose of eliminating delivered pricing. In fact, it is not accepted that they can significantly limit delivered pricing systems at all as they only have application where the saving gained from switching from the closest supply point exceeds the additional cost of transporting the goods from the new transport point. For example, where a buyer in one zone buys goods in another zone and transports them back himself. Only in a rare case could such provisions be applied to basing-point or delivered pricing systems\textsuperscript{38}.

Thus the current provisions and the proposed provisions do not substantially affect or significantly alter the legal status of price discrimination, which remains almost immune from legal restriction in Canada.

\textsuperscript{37} See Consumer and Corporate Affairs Amendments to the Combines Investigation Act: Background Information and Explanatory Notes pp. 22-23.

6.5 FRANCE

It is interesting to consider the approaches of France and West Germany to the problem of price discrimination. France has a history of carefully planned economic strategy facilitated by extensive state intervention. Competition policy has not been a high priority although the protection of small business is seen as integral to the development of the economy. Because of this, the stringent controls on price discrimination contained in the Loi d'Orientation du Commerce et du l'Artisanat (Act Regulating Arts and Crafts) of 1973 may be contrasted to the weak controls on monopolies and mergers. Section 37 reads:

37) No producer, trader, manufacturer or craftsmen shall
1. apply discriminatory prices or conditions of sale which are not justified by corresponding differences in the price of articles or services applied.
2. circumvent subsection 1 above by directly or indirectly giving any re-seller gifts in kind or in cash or free services.
A producer must furnish any reseller who so requests with his price lists and his conditions of resale.

38) No re-seller shall seek or knowingly accept from a supplier any benefits contravening section 37.

This has many similarities to the Irish approach. The emphasis on fairness, and the requirement that sellers publish their price lists in order to prevent circumvention of the Act with apparent disregard for the anti-competitive effects on price flexibility and inter-seller price fixing that such a publication may have. However, the French Act retains a simplicity that is lacking in the Irish Orders, mainly because the French have not felt the need to consider price flexibility in their Act.

6.6 WEST GERMANY

In comparison with the French approach, the Germans have
emphasized competition and have been reluctant to give fairness an elevated status. Their approach, similar to that of the English, has been to treat price discrimination as a form a monopolistic abuse. Section 26(2) of the Act Against Restraints of Competition (as amended in 1973) provides that:

Market dominating enterprises...shall not unfairly hinder, directly or indirectly, another enterprise in business activities which are usually open to similar enterprises nor, in the absence of facts justifying such differentiation, treat such an enterprise directly or indirectly in a manner different from the treatment accorded to similar enterprises. Sentence 1 shall also apply to enterprises and associations of enterprises, insofar as suppliers or purchasers of a certain type of goods or commercial services depend on them to such an extent that sufficient and reasonable possibilities of dealing with other enterprises do not exist.

This section deals with any type of abuse by market dominating enterprises or groups of enterprises, including refusals to supply and discriminatory dealing, if the buyer is in some way dependent on the seller. The section is not without problems and Grant identifies three areas of obscurity in the language:

(i) The relationship of dependence is not made clear,
(ii) it is not clear what facts may 'justify' a differentiation,
(iii) it is not clear how this section could control the abuse of buying power.

A 1977 Report by the Monopolies Commission stated "abuse by market dominating enterprises when applied to buyers does not present any difficulties that are fundamentally different from those which occur when applied to sellers"; although a 1980 Amendment was introduced.

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41 Fourth Act Amending the ARC (1980).
to make it clear that the Act could be applied to buyers. This amendment made it illegal for a market dominating enterprise or an enterprise with dependent suppliers to require another enterprise to grant unjustified preferential terms. It also allowed a presumption that a seller is 'dependent' on a buyer where the buyer "regularly obtains special benefits not granted to similar purchasers".

However, the Monopolies Commission has vehemently opposed a general ban on price discrimination:\(^\text{42}\):

There is no intention in the ARC to enact a general prohibition of discrimination, aimed at eliminating disadvantages suffered by the competitors of the major buyers in the retail sales market, because they obtain less favourable prices, discounts and terms in their purchasing. Such a prohibition produces negative economic effect because encouragement to purchase goods as economically as possible is excluded and the trend towards price competition as a result of investment competition is neutralised. A general prohibition of discrimination considered in isolation from differences in costs would immediately recreate hidden discrimination in the economic sense because it would compulsorily impose the same prices despite different supply costs. A prohibition which permitted an exception owing to the difference in costs would lead to prices being pegged to costs. Such a prohibition would be irreconcilable with dynamic price competition.

Despite the lack of clarity in the language, the German approach to the problem of price discrimination is highly commendable. It begins by recognising that price discrimination is a problem of monopoly and continues to provide a solution which addresses the problem in a consistent manner. It recognises that a monopolist has enhanced power and that all other firms in the distribution system then become dependent on that firm and it seeks to limit the ill effects of this dependency. Although it does not treat the monopoly problem itself, it is compatible with anti-monopoly legislation. Most important, it does

\(^{42}\) German Monopolies Commission, op. cit., "Summary of the Results", para. 18.
not seek to achieve fairness within competition by imposing a blanket ban on discriminations.
CHAPTER VII

PRICE DISCRIMINATION LEGISLATION IN NEW ZEALAND

7.1 HISTORY OF PRICE DISCRIMINATION LEGISLATION IN NEW ZEALAND

(1) Introduction

Currently there is no legislation in New Zealand aimed directly at price discrimination. The tendency to import legislation from other countries, especially from Australia, the United Kingdom and the United States, has not yet extended to price discrimination. An explanation for this is that small business remains healthy and therefore there has not been the same agitation for price discrimination legislation as in other countries.

The Commerce Act 1975 does contain provisions which may extend to price discrimination. The Commerce Act resulted from the consolidation of prior trade regulating statutes and is currently the only statute regulating anti-competitive practices in New Zealand. It replaces the Commercial Trusts Act 1910, an Act to prevent the growth of monopolies in New Zealand, and the Trade Practices Act 1958, which dealt with restrictive trade practices.

(2) The Commercial Trusts Act 1910

The Commercial Trusts Act 1910 was enacted to prevent the growth of monopoly in New Zealand. Two provisions dealt with the use of refusal to supply or refusal to supply except on discriminatory terms in order to further the objectives of a commercial trust. The refusal to supply or discrimination was proscribed even though it was ancilliary to another practice.
3. Every person commits an offence who, either as principal or agent, in respect of dealings in any goods, gives, offers, or agrees to give to any other person any rebate, refund, discount, concession, allowance, reward or other valuable consideration for the reason or upon the express or implied condition that the latter person -

(a) Deals or has dealt or will deal or intends or undertakes or has undertaken or will undertake to deal, exclusively or principally, or to such an extent as amounts to exclusive or principal dealing, with any person or class of persons, either in relation to any particular goods or generally; or

(b) Does not deal or has not dealt or will not deal or intends or undertakes or has undertaken or will undertake not to deal with any person or class of persons either in relation to any particular goods or generally; or

(c) Restricts or has restricted or will restrict, or intends or undertakes or has undertaken or will undertake to restrict, his dealing with any person or class of persons, either in relation to any particular goods or generally; or

(d) Is or becomes or has been, or has undertaken or will undertake to become a member of a commercial trust; or

(e) Acts or has acted or will act, or intends or undertakes or has undertaken or will undertake to act, in obedience to or in conformity with the determination, directions, suggestions or requests of any commercial trust with respect to the sale, purchase or supply of any goods.

4. Every person commits an offence who, either as principal or agent, refuses, either absolutely or except upon disadvantageous or relatively disadvantageous conditions, to sell or supply to any other person, or to purchase from any other person, any goods for the reason that the latter person -

(a) Deals or has dealt or will deal or intends to deal, or has not undertaken or will not undertake not to deal, with any person or class of persons, either in relation to any particular goods or generally; or

(b) Is not or has not been, or will not become or undertake to become or has not undertaken to become, a member of a commercial trust; or

(c) Does not act or has not acted or will not act, or does not intend to act, or has not undertaken or will not undertake to act, in obedience to or in conformity with the determinations, directions, suggestions or requests of any commercial trust with respect to the sale, purchase or supply of any goods.

The single successful prosecution under this Act involved offences under both S. 3 and S. 4. In The Merchants' Association of New
Zealand (Inc.) and Others v. The King\footnote{1}, the Colonial Sugar Company, by arrangement with an association of merchants and individual firms, issued a scale of discounts to be allowed on the purchase of sugar. The scale was framed so as to deny the maximum discount to those companies who were not members of the association. This was done by allowing a nominee of a group of affiliated merchants to purchase sugar on their behalf and thereby earn the maximum discount but the same buying privileges were denied to firms outside the group. The effect of the arrangement was to give the Association control over the distribution of sugar in the Dominion. The arrangement also had as one of its objectives the protection of the company from foreign competition. Clearly there was discriminatory conduct as discounts were given on condition that the recipient became a member of the trust (S. 3) and discounts were refused to a firm because that firm failed to comply with the directions of the trust (S. 4).

The Act fell into disuse after the King v. Crown Milling Co. Ltd decision\footnote{2}. Distributors Ltd was incorporated to act for six years as the selling agency in the home market for all the flour millers in the Dominion (with some small exceptions). The agreement amounted to the monopolisation of the flour trade in the country. A conservative Judicial Committee of the Privy Council found that the conspiracy to monopolise was not contrary to the public interest and therefore not a violation of S. 5. No violation of S. 3. was committed as Distributors Ltd, the controlling body, was not an 'other person' as required by the section but merely an agent of the millers. This decision rendered the monopolisation provisions of the Act impotent.

\footnote{1} Merchants Association v. R., [1913], 32 NZLR 537.

\footnote{2} [1925] NZLR 258 (S.C.); 753 (C.A.); [1927] A.C. 394 (P.C.).
(3) The Trade Practices Act 1958

No other antitrust statute was enacted until the Trade Practices Act in 1958. The lack of control following the demise of the Commercial Trusts Act 1910 may be attributed to the policies of government intervention in response to the Great Depression and World War II which made trade practices regulation unnecessary. The enactment of the Trade Practices Act 1958 can be seen as part of the movement back to a competition-based economy.

The structure of the Act was based in large part on the British Restrictive Trade Practices Act 1956. Those trade practices within the ambit of the 1958 Act were explicitly defined and a case by case evaluation of each trade practice was required; the criteria for disapproval being explicitly stated in the Public Interest test. As a result of amendments in 1961, 1965 and 1971, a threefold division of trade practices emerged. Some trade practices were considered lawful until shown to be contrary to the public interest, others were considered prima facie contrary to the public interest but capable of justification and some practices were per se illegal and incapable of justification.

The Trade Practices Act 1958 proved relatively successful in controlling restrictive trade agreements, especially as the interventionist policies of the 1930's and 1940's had taken much of the competitive vigour out of the economy and left many industries governed by trade associations eager to assume the regulatory role which government had abandoned. The cases that came before the Trade Practices Commission and the Appeal Authority served to sharpen understanding of Trade Practices regulation and many of those cases are still reliable precedents under the Commerce Act 1975.

The Trade Practices Act 1958 was repealed in 1975 although much of its structure and terminology is embodied in the Commerce Act 1975.
(4) The Commerce Act 1975

Competition law in New Zealand is now contained in the Commerce Act 1975. This Act consolidates the Trade Practices Act 1958 (and amendments) and The Control of Prices Act 1947 and makes specific provision for the control of monopolies, oligopolies, and mergers and takeovers.

Trade practices are dealt with in Part II of the Act while Part III relates to monopolisation, mergers and takeovers. Responsibility for enforcing the Act rests solely with the Examiner of Commercial Practices and there is no right of private action. The Examiner may initiate an investigation on his own motion, on a complaint made by a member of the public, or following a reference from the Department of Trade and Industry or the Commerce Commission. If the Examiner finds that a monopoly, oligopoly, merger, or trade practice is contrary to the public interest, (defined in Section 21 and Section 80), he may attempt reconciliation with the parties to the practice in order to remove any harmful effects. Failing this, he may instigate proceedings against the parties before the Commerce Commission.

The Commerce Commission is charged with the adjudication of the Act. The Commerce Commission has a wide range of remedies available to it. It may direct the discontinuance of a trade practice, allow the practice under certain conditions, or direct parties to revert to terms applicable before the trade practice was begun\(^3\). Where a proceeding is brought under the monopolisation provisions, the Commission has the power to order dissolution of the company or any part of it, to restrict the area where business is carried on, or order that the offending parties cease any business practice or method of trading\(^4\). Appeals may

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3 Commerce Act 1975, s. 22.

4 ibid, s. 65.
be made to the Administrative Division of the High Court.

7.2 THE CURRENT LEGAL STATUS OF PRICE DISCRIMINATION IN NEW ZEALAND

(1) Trade Practices under the Commerce Act

The threefold division of trade practices was carried over from the Trade Practices Act 1958. The list of examinable practices is contained in Section 23(1). The Section mostly refers to agreements or arrangements between competitors to restrict competition between them. Price fixing and resale price maintenance are both approvable practices, and collective tendering and collective bidding at auctions, tying arrangements, hoarding, black marketing, mandatory trade-ins, and profiteering are all prohibited practices.

(2) The Refusal to Supply Provisions

Of relevance to our topic is Section 23(1)(i) which defines an unjustifiable refusal to supply. Its provisions read:

23(1)(i) Subject to subsections (5) and (6) of this section, any unjustifiable refusal -
(i) By a wholesaler to sell or supply, or to continue to sell or supply, goods to a retailer, a manufacturer, or a supplier of services:
(ii) By a retailer to sell or supply, or to continue to sell or supply, goods to a manufacturer, or a supplier of services:
(iii) By a manufacturer to sell or supply, or to continue to sell or supply, goods to a wholesaler, a retailer, a manufacturer, or a supplier of services:
(iv) By a supplier of services to supply, or to continue to supply, services to a wholesaler, a retailer, a manufacturer, or a supplier of services:

The Subsection is expanded by section 23(5) which defines a refusal to supply as any refusal to supply except on discriminatory terms:

23(5) For the purposes of subsection (1)(i) of this section and without limiting the generality of that paragraph, a refusal to sell or supply, or, as the case may be, a refusal to continue to sell or supply, shall be deemed to
have occurred if there has been a refusal to sell or supply the goods or services, except at prices or upon terms as to discount, credit, or delivery, or upon product or service guarantee terms or upon other terms or otherwise, which -

(a) Are so disadvantageous as to be likely to deter the prospective purchaser from acquiring those goods or services; or

(b) Are higher or more onerous, as the case may be, than the prices or terms available to purchasers of the same class acquiring those goods or services in similar quantities under similar conditions of purchase.

This is the only direct reference to price discrimination in the Act. Several salient features of the section should be noted. It is a supporting provision of Section 23(1)(i) which relates to refusal to supply. In turn, a refusal to supply is often only ancillary to another trade practice such as price fixing or resale price maintenance. Thus, it was written with the 'hold-them-in-line' type of price discrimination in mind. Second, the practice is examinable and therefore a seller may grant discriminatory terms until the practice is proscribed by the Commerce Commission.

(3) Section 23(5)a

(a) The Meaning of 'Disadvantageous'. Section 23(5) contains two distinct tests. S. 23(5)a is a wide test with greater application to price discrimination. Under this test, a refusal to supply occurs where the terms granted to one buyer are "so disadvantageous as to be likely to deter the prospective purchaser from acquiring those goods or services".

The meaning of disadvantageous is not given in the Act. What is advantageous to some buyers, may be disadvantageous to others. This would be a subjective test based on the tastes or preferences of the buyers. A more objective test would be to assume that some situation is 'normal' or not disadvantageous, and a departure from this situation is disadvantageous. The situation prevailing prior to any change of terms,
or the terms granted to other purchasers, may be used as yardsticks to measure 'disadvantageous'. Although S. 23(5)a contains no explicit inter-period or inter-firm comparison tests, such comparisons are the only way of avoiding the quagmire of applying subjective tests of 'disadvantageous'.

Commerce Commission decisions in two cases involving discriminatory dealing have added some meaning to the term and confirmed the use of the comparison tests. In 

Bailies\(^5\), Philips and Pike (hereinafter referred to as P & P), an importer of liquor, refused to supply goods to Bailies, a wholesaler of liquor, unless the goods were delivered to that point where Bailies held their wholesale licence. Because of this policy Bailies was forced to accept delivery of its goods in Westport and then reship them to its major markets of Christchurch and Dunedin. P & P had recently instigated this policy with all wholesalers to whom it sold, although other wholesalers held their licences in major cities and therefore were not disadvantaged to the same extent as Bailies. The delivery policies of P & P were followed by other liquor manufacturers and importers. The Commission concluded that a substantial reason for this policy was to force Bailies to cease selling at discounted wholesale prices.

P & P was alleged to have refused to supply goods to Bailies except on terms that were so disadvantageous as to deter Bailies from purchasing the goods. The unique feature of this case was that the same terms were applied consistently by P & P to all wholesalers and thus it was not possible to make an inter-firm comparison. The Commission said:

\[209\]. The next question to be considered is whether these terms of delivery were so disadvantageous to Bailies as to deter it from ordering the goods. Bailies stated that the new terms were disadvantageous. Philips & Pyke did not directly argue that the terms were not disadvantageous to Bailies, but rather contended that its terms to Bailies

were the same as its terms to all its other customers and Bailies was therefore not in any different - or disadvantageous - position compared with these other customers. This highlights the two different approaches to the measure, or determination, of disadvantageous. Disadvantageous compared to what? Bailies compared its new position to its former position, and found a disadvantage in its new position. Philips & Pyke compared Bailies' new position to the new position of any other of its customers and found no difference - neither advantage or disadvantage.

The Commission agrees that the new terms were disadvantageous to Bailies in comparison with the previous terms, and accepts that they were disadvantageous to an extent which would deter Bailies from acquiring the goods.

In considering Bailies' position in comparison with any other of its customers, Philips & Pyke argued that Bailies was in no different position regarding its sales in Dunedin, for example, from a Dunedin wholesaler who wished to sell in Westport... The delivery arrangements imposed by Philips & Pyke may have treated both cases in the same manner but it cannot be accepted that it is correct to justify disadvantageous treatment to Bailies by pointing to equally disadvantageous treatment to all other customers. In other words, two wrongs do not make a right.

From this statement, we may conclude that comparison over time is a valid means of determining 'disadvantageous'. Unfortunately the conclusion is weakened somewhat by the argument in Para. 211. The Commission clearly felt that the terms to Bailies were imposed to dissuade Bailies from their discounting practices, that the new terms could not be justified, and that they were wrong. It is not so clear whether the Commission didn't mix 'disadvantageous' with 'justification', perhaps relying more heavily on the second test.

A second interpretation of S. 23(5)a was given in the Memorandum to Counsel in the Pints and Cans case. Dominion Breweries and Lion Breweries supplied pallets of beer direct from their Auckland premises to the Duke of Marlborough Hotel who delivered the goods to their premises in Russell. The Duke of Marlborough was charged wholesale

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6 Decision No. 52, dated 3 July 1981.
prices through a wholesaler, even though the wholesaler had no contact with the goods and the Duke of Marlborough performed the delivery function normally performed by the wholesaler. (The wholesaler did assume the credit function). In summary, the Duke of Marlborough was a direct-buying retailer who was denied the wholesale mark-up.

The Duke of Marlborough Hotel claimed that it was entitled to the same prices as a wholesaler (ex-brewery prices) because it performed the wholesale functions, and that the terms (wholesale prices) were so disadvantageous as to be likely to deter it from purchasing the goods. The Commission said:

From its calculations, based on current prices, the Commission notes that the 12.5 percent commission to a wholesaler on a pallet of "Double Brown" cans collected from the brewery store by the Duke of Marlborough would be $113.04 on a sale valued at $904.32. Similarly on a pallet of pint bottles the commission could be $55.50 on a sale worth $444. In the Commission's view these rates of commission on goods supplied by the brewery, requiring no direct participation by the wholesaler, cannot be sustained and are disadvantageous.

There was no scope for inter-period comparison in the Pints and Cans case, as the terms applicable to the Duke of Marlborough Hotel had remained constant over time. The decision may have been based on a comparison of the terms normally given to firms that performed the wholesale function (ie. ex-brewery prices), and the terms given to the Duke of Marlborough Hotel (ie. wholesale prices). If this interpretation is correct, then it may have several interesting implications. The inter-firm comparison would not have been between firms operating on the same functional level, but rather between firms that perform the same functions. The Duke of Marlborough was compared with wholesalers even though the hotel was a retailer. Thus a firm which integrates vertically could receive the functional discount applicable to its highest level of operation, (compared with the present American law which allows discounts based on the lowest level of operation).
Unfortunately, one cannot help but get the impression that the Commission found the mark-up 'unjustified' (or unsustainable) and therefore disadvantageous, again mixing the two tests.

Finally a brief consideration of the term was given in the Order that followed a refusal by Richardson-Vicks Limited to supply Oil of Ulan to L.D. Nathans Ltd, (Woolworths and Maximart stores)\(^7\). There had been no supply for over 4 years so there could be no inter-period comparison. The Commission ordered Richardson-Vicks to supply the goods to L. D. Nathans on terms that were not 'disadvantageous': "the Commission's view is that, at the least, it would not expect Nathans to receive terms less favourable than those accorded to other purchasers for comparable quantities and terms in comparable circumstances".

(b) **Degree of Disadvantage.** When are terms so disadvantageous "as to be likely to deter the prospective purchaser from acquiring those goods or services"? The Commission has ruled that the terms need not be so disadvantageous as to cause supply to cease altogether to fulfil the requirements of the section. (Neither the Duke of Marlborough nor Bailies has ceased purchasing altogether).

The only indication of the necessary level of "disadvantageous" was given in **Pints and Cans** where the Commission said:

27.....the prices charged are a deterrent to the Duke of Marlborough which is restrained by them in its purchasing, having regard to its potential for sales in the area. (emphasis added).

This comment is interesting as it indicates that a buyer is deterred from purchasing the goods or services if the disadvantageous terms affect the quantity in which he buys and sells. Higher buying terms will almost always deter a buyer and reduce his sales and thus the requirements of the section will automatically be fulfilled. However, if the disadvantage is not substantial enough to affect the buying and

\(^7\) Decision No. 111, dated 14 February 1985.
selling patterns of the buyer, then it will be considered de minimus and not subject to the Act's proscriptions.

(4) **Section 23(5)b.**

The second limb of S. 23(5) contains a comparison test which more closely resembles the tests used in the Robinson-Patman Act and the Australian Trade Practices Act 1974. Section 23(5)b applies where discriminatory terms are "available to purchasers of the same class acquiring those goods or services in similar quantities under similar conditions of purchase".

(a) **The Meaning of 'Class'.** The meaning of this subsection was extensively discussed in the *Pints and Cans* case by the Counsel for Dominion Breweries, Mr John Collinge. The meaning of "purchasers of the same class" was given particular consideration in those submissions. Some alternative definitions of 'class' were canvassed:

(i) The definition contained in the licence of the Duke of Marlborough in accordance with the Sale of Liquor Act.

(ii) The definition contained in S. 23(2) or S. 2(1) of the Commerce Act 1975.

(iii) The retail function of the Duke of Marlborough, with consideration given to the proportion of sales made by the Hotel at the wholesale level.

(iv) The level at which the Hotel purchases goods, defining the functions performed by the Hotel.

The Commission explicitly rejected Option 1. But unfortunately no further clarification of the term was given as the Commission relied on 23(5)a to establish jurisdiction. This may represent an implicit rejection of Option 4 and acceptance of either option 2 or 3; this forcing the Commission to establish jurisdiction by this alternative means.
(b) The Meaning of 'similar quantities under similar conditions of purchase'. No cases have discussed the meaning of 'similar quantities under similar conditions of purchase' although similar language was used in the Richardson-Vicks Order. The Commission also used the language in a decision concerning the merger of Winstones Ltd and Odlins Ltd. The merger had both horizontal and vertical implications and the Commission expressed concern for those independent purchasers left in the market. One condition attached to the merger was:

In respect of the sale of goods ....by it, Winstone shall not discriminate between any purchasers of the same class acquiring such goods in similar conditions of purchase and Winstone operations or divisions of the same class acquiring these goods in similar quantities and under similar conditions of purchase [except solely on identifiable economic grounds] or between purchasers of the same class outside the Winstone group acquiring such goods in similar quantities and under similar conditions of purchase. These undertakings shall apply to normal and regular supply and delivery, terms and conditions of sales, prices, discounts and credit terms. It is acknowledged that Winstone may adjust prices and terms of supply to meet specific market conditions.

Purchasers would be distinguished if the quantities or conditions of purchase differ sufficiently to affect the costs of the seller. The term 'conditions of purchase' relates to the conditions of the sale contract between the seller and the buyer. Purchasers may be distinguished if they accept different terms of credit, delivery or storage, etc. It should not serve to distinguish customers merely because they redistribute goods by different means or operate on different functional levels.

If quantities or conditions differ significantly, then sales are not comparable and the section cannot be applied. This is a weakness similar to the 'like quantity' test found in the original Clayton Act.

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(5) **Other Jurisdictional Elements**

Section 23(1)(i), as extended by Section 23(5), is applicable to the practice of price discrimination. The provisions of Section 23(5) (a) and (b) clearly allow the terms of purchase granted to two buyers to be compared to see if one has received discriminatory treatment. Section 23(5)b requires the two sales to be reasonably similar, while the term 'disadvantageous' places no restriction on the type of discrimination that can be caught under 23(5)a and this avoids many of the rigidities that have occurred through the equation of 'discrimination' and 'difference'.

However, Section 23(5) is directed at the 'hold-them-in-line' type of price discrimination and may be applied to ensure that there is a free flow of goods or services from the seller to the buyer. Because of this, the section is not well suited to catch other forms of price discrimination.

It applies only to the seller and places no liability or penalty on the buyer who induces a discrimination. This is consistent with the objective of ensuring the supply of goods to the disfavoured buyer and the section was never intended to apportion blame or apply penalties. However, this places a seller subject to a Commission Order to treat buyers equally in the unfortunate position of being caught between the law and the large buyer. Also the section is aimed at the flow of goods between market participants such as manufacturers, wholesalers and retailers, and does not apply where the seller supplies to a consumer (who does not resupply the goods). Thus it cannot be applied to cases of predation at the retail level.

In other areas, the jurisdiction of the section is wide. It applies to refusals to sell, offers to sell and executory contracts. (Section 2(4) deems the publication or exhibition of a price list to be an offer to sell on terms specified in that price list). It is
considered that a seller must *actively* refuse to grant the buyer favourable terms and the mere publication of a price list containing disadvantageous terms will not constitute a refusal to sell except on disadvantageous terms within the meaning of the section.

Non-sale transactions are also caught under the section, 'supply' being given an expanded meaning in Section 2(1) to include sale, exchange, lease, hire, or hire-purchase.

The section applies to the supply of goods and services. No attention has been given to whether goods must be identical or merely of 'like grade and quality' before comparison of terms can be made. Section 2(3) deems goods to be "of the same kind as other goods if they are in fact of the same nature and quality, or if they are substantially of the same nature and quality". Thus a seller must treat buyers equally if they buy goods of substantially the same nature and quality. There have been no cases on the meaning of that term.

A discrimination may occur in "prices or upon terms as to credit, discount, delivery, or otherwise". Price is already widely defined in Section 2(1) as "any valuable consideration whatsoever, whether direct or indirect", and in *Bailies* the Commission was prepared to give a wide interpretation of 'price' to catch terms of delivery⁹. Following that first decision, the section was explicitly expanded by the Commerce Amendment Act (No. 2) 1979 to include discriminations relating to "discount, credit, or delivery, or upon product or service guarantee terms or upon other terms". Promotional allowances and other forms of indirect discrimination should easily be caught within the section.

Two defences are implied in Section 23(5). If goods or services are 'available' to all buyers on equal terms there isn't the requisite refusal to deal. The changing conditions defence is implicit in the any

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⁹ Decision No. 40, dated 20 August 1979.
comparison between two buyers as such a comparison assumes that external conditions have remained constant. In the event of changing market conditions or the changing marketability of the goods, any inter-firm or inter-period comparison is invalid. Also perishable goods should not be considered of the same 'nature and quality'.

(6) **Justifying Price Discrimination**

Once a refusal to deal has been established under Section 23(1)(i), the party refusing to supply the goods or services may show that the refusal was "justified". The meaning of this term was clarified by Mr. Justice Dalglish in the **Kemphorne Prosser** case, who declined to accept that a refusal was justified if it was not proscribed by the law, and instead stated\(^{10}\):

> A refusal to sell or supply goods is 'unjustifiable', within the meaning of that paragraph, when the party seeking to uphold it is unable to establish that it was done for reasons which accord with justice or fairness. Any discriminatory treatment that cannot be 'justified' will certainly be considered unfair.

The most obvious justifications of price discrimination are the cost-justification and meeting competition defences, and, if not implicit elsewhere, the changing conditions and availability defences. Because there is no language relating specifically to these defences, it is likely that they will be given liberal application as the Commission tries to distinguish pricing practices which are "fair" from those which are "unfair". Showing that any one of these defences applies, or was believed to apply at the time the discrimination was granted, should be sufficient to show that the seller acted in accordance with justice and fairness.

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\(^{10}\) Re Kemphorne Prosser and Co.'s New Zealand Drug Co. Ltd, decision of the Appeal Authority, [1964] NZLR 49, p. 52.
Despite the flexibility which may seem to occur because of the lack of specific attention to these defences, it is believed many of the rules applied in Robinson-Patman cases will be transferred to our justification defence. For example, the meeting competition defence may be restricted to 'meeting' and not 'beating' competition, as to deliberately undercut a competitor would not be considered 'fair'. Similarly, acceptable cost data should be presented to verify cost-justified discounts. Thus the ambiguity of the justification defence does not avoid all the rigidities found in the Robinson-Patman Act.

The breadth of the 'justification' test may allow other means of justification based on trade practice or injury to the seller. Volume and quantity discounts may be sustained if they are common to an industry and are considered normal trade practice. (Here we are returning to a case similar to meeting competition using pricing systems).

This idea was tested in Pints and Cans where Collinge, on behalf of Dominion Breweries, argued that the practice of giving lower prices to wholesalers than is given to retailers such as the Duke of Marlborough Hotel was common trade practice and was therefore justified. The Commerce Commission was unsympathetic and felt that trade practice of granting functional discounts did not justify charging a wholesale mark-up where no wholesale function was performed.

The argument that a firm was meeting competition may also not be successful where the discriminatory practice resulted from the firm's initiative. Thus a dominant firm whose practices are adopted industry-wide may not claim that he was merely following normal industry practice.

Another way in which the seller may claim justification is by showing that he would be harmed but for the discrimination. He may claim that a large buyer had induced the discrimination and he was justified
in submitting to this pressure. This is a persuasive argument and should be sufficient to justify the seller's actions. In such a case, it seems better to charge a buyer with monopsony rather than pursue the seller.

(7) The Monopolisation Provisions

The monopolisation provisions of the Act provide an alternative means of attacking price discrimination. The provisions were strengthened in the Commerce Amendment Act 1983, and now extend to conduct as well as structure as is shown by S. 61:

61(1) Where it appears to the Examiner-
(a) that there may exist in New Zealand or in any part of New Zealand-
(i) Any monopoly or oligopoly of the supply of any goods or services or of any particular discription of goods or services or of both goods and services; or
(ii) Any circumstances that are tending or may tend to bring about any such monopoly or oligopoly; and
(b) the existence of that monopoly or oligopoly, or of those circumstances, or any conduct of that monopoly or oligopoly, may be contrary to the public interest in terms of section 80 of this Act, -
he may conduct an investigation into the existence of the monopoly or oligopoly, or those circumstances, or that conduct.

Definitions of monopoly and oligopoly are contained in S. 2:

2) "Monopoly" means a situation in which a person, either alone or together with any inter-connected body corporate (as defined in section 67(6) of this Act), is in a position to substantially control or exercise a predominant influence over a market for goods or services or of any particular description of goods or services in any part of New Zealand; and includes a situation in which a person, either alone or together with any inter-connected body corporate (as defined in section 67(6) of this Act), has by reason of his or their share of the market or technical knowledge or access to raw material or capital, the power to determine the prices or to control the production or provision or distribution of a substantial part of any goods or services or of any particular goods or services in any such market:

"Oligopoly" means a situation in which a market for goods or services or both or a large part of a market for goods or services or both is supplied by a small number of distinct businesses:
The definition of monopoly is derived partly from the Continental Can case decided by the European Court of Justice in respect to Article 86 of the Treaty of Rome\textsuperscript{11} and is similar to the definition adopted in the Australian Trade Practices Act 1974\textsuperscript{12}. A seller who engages in price discrimination (in the economic sense), \textit{ipso facto}, has power to determine prices in some part of the country and should automatically fall within the definition of monopoly. Similarly a buyer who is powerful enough to induce a price discrimination must have some monopsonic power and would also fall within the definition of monopoly.

No cases have been decided to clarify the meaning of the provisions and this may have prompted the 1983 Amendment which allowed the Commission to consider whether the conduct of the monopolist or oligopolists was contrary to the public interest. Prior to these amendments the Commission had to evaluate whether the monopoly or oligopoly \textit{as a whole} was contrary to the public interest. The focus on particular conduct rather than structure allows the Commission to eliminate anti-competitive conduct without assuming the awesome task of evaluating the monopoly itself.

The scope of the monopolisation provisions is wide. The term "conduct" will include any price discrimination by a monopolist, the reference to oligopolies may allow concerted behaviour such as delivered pricing to be caught, and systematic price discrimination may be considered a "circumstance" tending to bring about a monopoly or oligopoly. Thus, as with S. 23(5), there does not seem any difficulty in establishing jurisdiction over discriminatory pricing.

Although there are no explicit defences and no justification test is provided, it is likely that the defences of cost justification, \hfill


\textsuperscript{12} Trade Practices Act 1974, S. 46(3)
meeting competition, availability and changing conditions are implicitly available, giving the seller the same opportunities to justify a discriminatory practice as under section 23(1)(i).

If a buyer were charged with abuse of buying power, it is interesting to ask how he could justify inducing a discriminatory discount. Bargaining for discounts is a normal and accepted commercial practice but it is a matter of conjecture whether the Commerce Commission will allow the abuse of buying power simply because it is a normal part of competition. There are good reasons why such abuse might be brought within the ambit of the Act:

(i) there is no explicit defence allowing a buyer to induce discriminatory discounts simply because it is normal business practice, and

(ii) the purpose of the monopolisation provisions is to prevent the flagrant abuse of power and to prevent further concentration. The inducement of discriminatory discounts violates both of these aims.

The Commission may limit its jurisdiction by requiring that the buyer knew the discounts were discriminatory. This would represent a reasonable compromise between exempting all abuses because they are normal practice, and preventing all abuses because they are examples of monopsonistic power.

Where delivered pricing systems and other pricing systems practiced industry-wide by oligopolists are examined under the provisions, the Commission may reject the meeting competition defence and the reciprocity argument. Again, the provisions were intended to include tacit collusion in an oligopolistic industry and it seems reasonable to prevent such easy circumvention of the Act.
(8) **Price Discrimination and the Public Interest**

Once the Examiner succeeds in establishing jurisdiction over the trade practice, either under S. 23(1)(i) or under the monopolisation provisions, he must show that it is contrary to the public interest. For trade practices, the public interest test in contained in S. 21:

21. **Trade practices deemed contrary to the public interest** -

(1) For the purposes of this Act, a trade practice shall be deemed contrary to the public interest only if, in the opinion of the Commission, the effect of the practice is or would be -

(a) To increase the costs relating to the production, manufacture, transport, storage, or distribution of goods, or to maintain such costs at a higher level than would have obtained but for the trade practice; or

(b) To increase the prices at which goods are sold or to maintain such prices at a higher level than would have obtained but for the trade practice; or

(c) To hinder or prevent a reduction in the costs relating to the production, manufacture, transport, storage, or distribution of goods, or the prices at which goods are sold; or

(d) To increase the profits derived from the production, manufacture, distribution, transport, storage, or sale of goods, or to maintain such profits at a higher level than would have obtained but for the trade practice; or

(e) To prevent competition in the production, manufacture, supply, transportation, storage, sale, or purchase of any goods; or

(f) To reduce or limit the competition in the production, manufacture, supply, transportation, storage, sale, or purchase of any goods; or

(g) To limit or prevent the supply of goods to consumers; or

(h) To reduce or limit the variety of goods available to consumers or to alter, restrict, or limit, to the disadvantage of consumers, the terms or conditions under which goods are offered to the consumer.

A party to the trade practice may show that, notwithstanding that it has effects under one of these subsection, the effects are not unreasonable (S. 21(2)b), or that the practice has benefits to the public which outweigh its detriments (S. 21(2)a).

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The public interest test which is applied in monopolisation cases is found in S. 80. This test contains Section 21(1) in its entirety although the unreasonableness and balancing tests are omitted, and lists a pot-pourri of other considerations. The test reads:

80. In determining for the purposes of this Part of this Act whether the existence of any monopoly or of any oligopoly or of any circumstances that are tending to bring about any monopoly or oligopoly, or any conduct of any monopoly or oligopoly, ... is or is likely to be contrary to the public interest, the Commission shall have regard to -

a) The occurrence or likely occurrence of one or more of the effects described in S. 21(1) of this Act; and

b) The extent to which the monopoly, oligopoly, circumstances... does or would assist or hinder the promotion of -

(i) The interests of consumers, purchasers, and other users of goods and services in respect of the prices charged for goods and services or in respect of the quality or variety of goods and services supplied;
(ii) The development of industry and commerce (including regional development) in an effective and efficient manner;
(iii) The better utilisation of resources (including labour resources) or the enhancement of work skills and employment opportunities;
(iv) The reduction of costs and the development and use of new techniques and new products and the improvement of productivity;
(v) The entry of new competitors into existing markets;
(vi) Export trade;
(vii) Any other effects aiding the well-being of the people of New Zealand; and

c) The interest, in their capacity as employees, of any persons employed by any business or company which is directly affected.

Both public interest tests have similar features. Both direct the Commerce Commission to consider whether the practice has detriments under S. 21(1), although these are the only detriments which the Examiner may show if he proceeds under S. 23(1)(i). If he proceeds under the monopolisation provisions he may show the practice has detriments under any one of the listed categories. Both tests also allow the parties to provide evidence of public benefits and there is no limitation on the type of benefit which may shown.
The tests focus solely on effect of the trade practice and the purpose is irrelevant to the determination of public interest. The Commission may also consider the present and likely future effects of the practice.

Evaluating price discrimination under the public interest test becomes very complicated because the test is not confined to the effect on competition, as it is in the United States, and there is a multitude of other considerations which may be argued to show the practice either has detriments or benefits. Also profit maximising price discrimination may be caught within the jurisdiction of the Act even where it has no impact on competition. However, in the past the Commerce Commission has given a flexible interpretation to S. 21(1)f which refers to a detrimental effect on competition and it is likely that the Examiner will continue to rely on that subsection when establishing public detriments. We would assume that the Examiner would give priority to those cases where the practice harms competition.

When assessing the effects of price discrimination, the Commerce Commission may consider the aggregate effects of all discriminations given by a seller or obtained by a buyer.

(a) The effect on costs, prices and profits: The 21(1) a - d detriments. Section 21(1) a - d directs the Commission to consider the effect of the practice on prices, costs, or profits. The Section does not say whose prices, costs, or profits should be considered although this point was addressed in NZSSA where the Commission indicated that

14 Re the Passenger Agency Agreement of the Australian and New Zealand Passenger Conference. Decision No. 14 of the TPPC, dated 1 February 1963; decision of the TPAA, 20 August 1963.

15 Although see Kempthorne Prosser,[1964] N.Z.L.R. 49, where the Appeal Authority noted that the mere speculation of detrimental future effects could not sustain a violation of the Act.

16 Re An Application by New Zealand Stock and Station Agents Association. Decision No. 27 Para. 44
they would consider the effect of a trade practice on either the industry as a whole or on individual members of the industry.

The Commission might have to draw several conclusions before it could find that the practice has a detrimental effect on prices and costs. First, in the absence of discriminatory pricing, the seller would revise his pricing policies in such a way that the effect would be to lower prices to some firms.

But even this conclusion, standing alone, may not be sufficient to establish a 21(1) a - c effect if the Commission chooses to widen its focus to the whole industry rather than to a single competitor. This is so because it is not always correct to assume that the only effect of eliminating the discrimination is to lower prices to the disfavoured buyer. The seller may simultaneously increase prices to other buyers. Indeed, the Swanson Committee noted that one of the immediate effects of banning price discrimination was to raise prices and one criticism of the Robinson-Patman Act is that it adds to inflation.

Consider the most common form of price discrimination - where a seller grants a large buyer a discriminatory discount. Does the trade practice raise prices or costs? What is the effect absent the trade practice? The seller may -

(i) raise the price to the large buyer to match the price paid by the small buyer, possibly running the risk of losing the custom of the large buyer,

(ii) charge some 'in-between' price, again possibly losing the large buyer,

(iii) charge lower prices to the small buyers to match that given to the large buyer, and face a decline in profits.

Option 1 leads to higher over-all prices. Option 3 is likely only

\[\text{Supra, pp. 276-277.}\]
where you have a buyer so powerful that the pressure he exerts forces
down prices to all buyers. This is an unlikely result. Option 2 is the
most likely result of requiring uniform prices to all buyers, and it
would seem the net effect on prices is ambiguous.

The Commission might prefer to consider the general effect of
eliminating price discrimination on all firms buying from the seller.
Thus the Commission may have to balance the lower prices to some firms
against the higher prices to others.

Finally, the Commission may consider the effect on prices to the
public. The Commission would have to conclude that where price discounts
were given to some firms, these discounts would be passed on to the
consumer. Many small firms compete in terms of service and often a
discount received by them would be reflected in lower prices. In such a
case, the effect of requiring uniform prices is higher prices to the
consumer.

The beginning point of our investigation is whether the effect of
the practice on prices to individual firms, on all buyers or on the
public will be considered. Commission decisions provide some
illuminating, but somewhat confusing, answers on this question.

A narrow concern for the welfare of an individual competitor can
be seen in the Bailies and Pints and Cans cases, both involving issues
of price discrimination. In Bailies the Commission found that the
practice of delivering only to the location where the licence was held
had the effect of:

(i) increasing Bailies' cost of transport, stock holding and
financing charges, 21(1)a;

(ii) increasing the price of goods sold by Bailies to one of its
customers, Glenleith, 21(1)b;

(iii) increasing the price of goods sold by Glenleith to its
customers, 21(1)b;

(iv) hindering a reduction in prices at which goods were sold by
Bailies to Glenleith, and by Glenleith to its customers, 21(1)c;

(v) hindering a reduction in the costs which Bailies incurred in
the transport, storage and distribution of the goods Bailies purchased
from Philips and Pike, 21(1)c;

(vi) preventing competition in the purchase of goods by
Glenleith, 21(1)e;

(vii) preventing competition in the sale of goods from Bailies to
Glenleith, and from Glenleith to its customers, 21(1)e;

(viii) preventing Bailies competing with other wholesalers,
21(1)e;

(ix) limiting or reducing competition in the wholesale trade by
Bailies in Dunedin and Christchurch, 21(1)f.

Many of these findings are a corollary of each other.

The ease with which the Commission found these detriments is
suprising when it is considered that there were many alternative sources
of supply of liquor (including gin, the subject of this case) to the
retail market and there was no evidence of a horizontal agreement at any
level of distribution. Hence it is not clear how this trade practice
affecting such a small portion of the liquor trade could harm the
consumer. The Commission decision detailed the effect of the trade
practice on Bailies and its retailer-customer Glenleith and deemphasized
the general effects on the trade and on consumers.

The emphasis on competitors can also be seen in the Pints and
Cans case. The memorandum to Counsel reads:

28. It was claimed by the Examiner and the Duke of
Marlborough that the practice was contrary to the public
interest in terms of section 21 of the Act. In particular
it maintained costs and prices to the hotel at levels
higher than would otherwise obtain (sections 21(1)(a) and
(b)) and prevented the hotel reducing prices and limited
its ability to compete in areas in which it had traditionally operated (sections 21(1) (c) and (f)).

30. The Commission has concluded a case has been established against Lion and Dominion that their practice is unjustified and that it is contrary to the public interest in that it affects the prices at which the Duke of Marlborough must buy and sell, and consequently affects competition in and around the town of Russell.

It is submitted that the Commission would be acting contrary to the objectives of the Act if it were to concern itself solely with the effect of discrimination on the prices on individual competitors without weighing the net effects of the discrimination on all buyers. Where price discrimination leads to lower overall prices in an industry, concern for the individual competitor would be myopic and would contribute to inflation.

It is also submitted that the Commission's view in Bailies and Pints and Cans is not inconsistent with the wider concern with industry-wide prices. These cases are exceptional in that the Commission was easily able to conclude that prices to the disfavoured buyers would fall in the absence of discriminatory pricing without a concomitant rise in prices to other buyers. In Bailies, the practice was intended to and did have the effect of raising the costs of Bailies and no associated benefits were given to other buyers. This typical 'hold-them-in-line' discrimination tends only to increase prices and costs. In Pints and Cans, the Commission was concerned for the prices available to the Duke of Marlborough Hotel and the order was confined to that Hotel. Thus the Commission demanded only very limited non-discriminatory pricing and industry prices in general were not affected.

The Bailies and Pints and Cans cases are unusual in that they allowed an easy inference on the effect of the trade practice on prices and costs. In the more common situations where price discrimination arises, the effect of abandoning the practice is unclear and there may
not be sufficient evidence to support any firm conclusions. It is recognised that the Commission is entitled to infer effects from proven facts surrounding a trade practice and this has been accepted by the Appeal Authorities\(^{18}\). However, the High Court decision in the \textit{HANZ} case\(^{19}\), although considered a departure from the normal standards required, did indicate that there must be strong evidence to support an argument that prices or costs would be lower but for the trade practice. It is interesting to see whether the Commerce Commission will require the same high standard of proof as was required by Davidson J in \textit{HANZ}.

In conclusion we can see two (related) problems with determining that price discrimination has an effect on prices and costs which is contrary to the public interest. The first is that discriminatory pricing usually has either an ambiguous or favourable effect on prices and costs. The second is that the Examiner must provide adequate evidence of the effect of the practice on prices and costs. Usually such evidence is not available to him. Thus, a finding that price discrimination raises prices and costs does not follow automatically once discriminatory pricing is established, and the Bailies and Pints and Cans cases do not allow an automatic inference.

The question of whether price discrimination raises profits under S. 21(1)d is interesting. Economic theory indicates that this will always be the case as a seller will not discriminate unless it achieves his objective of profit-maximisation. The Commerce Commission has never fully accepted abstract economic theory and has preferred to base its findings on verifiable information. Again there may be no easy inference

\(^{18}\) See Hampton, \textit{op. cit.}, p. 225 and cases cited therein.

\(^{19}\) Re Hotel Association of New Zealand, Unreported Judgement (High Court, Wellington, M326/378, 4 March 1980, Davidson C.J.).
that the price discrimination is contrary to the public interest unless there is positive proof that the practice does raise profits.

(b) **The Effect on Competition.** Price discrimination can injure competition either at the primary line, the secondary line, or at some lower level of distribution. Where price discrimination is used in conjunction with predatory tactics to injure competitors of the seller, then the effect of the practice is usually to harm competition as a whole. Predation will normally be found to be injurious to competition.

If secondary-line competition and beyond is to be protected, the Commerce Act 1975 must be able to deal with injury to competitors, even where there is no injury to competition. Discounts given to some buyers but not to others often do not have an immediate or significant impact on competition. Although they might raise concentration levels, this effect occurs over a long period of time and is often not discernable because the discrimination is intermingled with many other causes for the concentration.

The difficulty of finding actual injury has forced the **Morton Salt** type of inference to injury. It is not certain whether the Commerce Commission will use a similar low threshold of injury. The decisions in **Bailies** and **Pints and Cans** seemed to allow such a low threshold although there are peculiar circumstances in both cases. Both cases were in the Liquor Industry which has been heavily regulated by government. As a consequence distribution in the industry is very structured and pricing is often not very aggressive. In **Bailies**, injury to Bailies and its retailer-customers may be synonymous with injury to competition even though there were many other wholesalers and retailers operating in the market. Bailies itself had earned a reputation for aggressive pricing. The Commission addressed this point:
261. The volume of business between Philips & Pike and Bailies formed only a very small part - about 2.5% in 1978 - of Philips & Pike's total sales of Beefeater gin. It was therefore suggested that the effects of this small level of trade were virtually insignificant in relation to the total liquor industry. However small it might have been in the eyes of Philips and Pike, it clearly formed a much more important part of Bailies' business. The Commission is also conscious that the implications of the practice are much wider than the effects between the immediate parties. (emphasis added).

In the Pints and Cans case, the Duke of Marlborough was the sole hotel in Russell although there were other smaller licensed premises such as boat clubs, etc. The injury to competition seems to have occurred because the Duke of Marlborough could not supply liquor to those other licencees who would, in turn, compete with the Duke of Marlborough. Thus the injured party was not the Duke of Marlborough Hotel but its competitors. The size of the geographic market and the lack of competitors played an important role in this case.

Therefore although a broad competition test is likely to be applied, in some instances industry conditions will demand a narrower test. If the disfavoured firm contributes to the competitiveness of the industry, as did Bailies and the Duke of Marlborough, then the price discrimination harming that firm will cause injury to competition in that market. In these cases injury to competition is synonymous with injury to certain competitors.

This reconciles Bailies and Pints and Cans with HANZ, and earlier decisions under the Trade Practices Act 1958 such as Master Grocers and Passenger Conference, where it was indicated that the trade practice must affect a substantial portion of the industry and not merely cause injury to a particular competitor.

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21 In re Australia and New Zealand Passenger Conference's Agreement, unreported decision of the Appeal Authority dated 20.8.63.
The broader competition test was used in Animal Remedies, a case decided under the 1958 Trade Practices Act, which has surprisingly similar features to the Bailies case and provides an interesting comparison. In Animal Remedies, thirteen farmers co-operatives alleged they were refused supply of broad spectrum drenches from three manufacturers. The co-operatives desired direct supply so they could pass on the profits to their members. Four major issues were canvassed: whether there was a refusal to supply, whether the co-operatives were retailers, whether the refusal was justified, and whether the refusal caused injury to competition. The Trade Practices and Prices Commission based their decision on the last issue. They found that there were many alternative sources of supply and that the refusal should not significantly affect competition in the retailing of the drenches. We have a situation, very similar to Bailies, where there was a large variety of sources of supply and no explicit price fixing agreement yet there was an implication that competitive forces had not not forced prices to their lowest level. The opinion differs in that Bailies was seen as a necessary pro-competitive force while the co-operatives were not. The reason for this dichotomy is not altogether clear. The case does show that competition rather than competitors is the concern of the Act.

Finally for the purposes of determining whether the effect on competition is 'unreasonable', section 21(4)b of the Act requires the Commerce Commission to consider the portion of total demand affected by the discrimination. Also the objectives of the Act in Section 2A and the long title of the Act both indicate that competition is the concern of the Act. These seem to militate against the use of a narrow competition test.

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22 In re Supply of Animal Remedies, Decision No. 34, TPPC, dated 5 February 1971.
(c) Other Considerations. If the discrimination is treated as a trade practice and considered under the S. 21 Public Interest test, the parties have the option of showing that the practice either provides benefits that outweigh the detriments or that it is not unreasonable. Under Section 80 either the Examiner or the Parties to the practice may argue that the practice has effects in any of the categories listed in section 80 (b) or (c).

Where there is primary line injury, the practice is likely to injure the employees of the victimised firm and generally harm the development of industry, technology, export trade, etc. It may discourage new entrants to a market and raise barriers to entry. In short, predation is unlikely to have any redeeming features.

Where the injury is to secondary line competition or beyond, the effects of the practice would probably be so long term that it is impossible to claim any benefits or detriments. It may be argued that price discrimination increases the supply of goods, or that it allows discounts to some buyers which would not have been given but for the practice and this in turn benefits consumers.

Where the discrimination ties a large buyer to a particular buyer there may be benefits in planning and productivity. It might also be argued that increased concentration levels allow firms to produce at more economic levels, compete more effectively in the export trade, or allow better regional development.

Arguments claiming any benefit or detriment should be verifiable, as it is unlikely the Commission would accept vague arguments to overcome positive proof of detriments.

(9) Conclusions.

Several features of the Commerce Act 1975 make it particularly amenable to control price discrimination. The jurisdictional tests
contained in the refusal to supply and monopolisation provisions are
broad and allow almost any form of price discrimination to be caught.

Another attractive feature is that the Act doesn't discourage
pricing flexibility. This is because price discrimination is an
examinable practice, higher standards of injury are required to prove a
violation and there is no provision for private enforcement or heavy
penalties. Therefore a seller may price his products freely until
ordered otherwise by the Commission.

However, the Commerce Act 1975 is a very limited tool to control
price discrimination for three reasons. First, S. 23(1)(i) (and
supporting provisions) are designed to deal with the 'hold-them-in-line'
form of price discrimination. As yet, the Examiner has not used the
section to attack price discrimination resulting from the abuse of
buying power and it remains to be seen if this self-imposed limitation
will continue.

A second self-imposed limitation is the reluctance to enforce the
monopolisation provisions. This may be because of the limited resources
of the Examiners Office and the vast resources required to successfully
combat a monopolist. Since the enactment of the Commerce Act 1975 no
cases have been pursued under these provisions and no change in attitude
has appeared following the Commerce Amendment Act (No. 2) 1983 which
made the provisions more accessible to the Examiner.

A third limitation of the Commerce Act 1975 is the high standards
of injury which must be shown. Although these high standards are
appropriate in primary line cases, price discrimination is most
commonly practiced without any designs on competition. It is symptomatic
of monopoly but generally does not significantly contribute to that
monopoly power.

The Commerce Act 1975 is not suited to deal with the large buyer.
There is rarely any immediate or measurable public detriment, no
noticable trend in concentration (if such trends occur at all) or unambiguous effects in prices, costs and profits. Many forms of price discrimination have innocuous effects on the general public interest and the Commission has not been persuaded to protect individual competitive situations. Thus, according to current criteria, there is no scope under the Act for these forms of price discrimination to be prevented.

These limitations neutralize the ability of the Act to control price discrimination. Those cases that have come before the Commission have been distinctive because they have concerned a particularly important or vigorous competitor in the market. They would be considered unusual price discrimination cases and do not offer hope to the small trader faced with a large competitor receiving discriminatory discounts.

7.3 REVISION OF THE COMMERCE ACT 1975

(1) The Proposed Revision

It is understood that the Commerce Act will be substantially revised. A new Commerce bill is in the legislative pipeline which, it is believed, will bring our law more in line with the Australian law. Expected changes are:

(i) the refusal to supply provisions will exist only as supporting provisions to the Resale Price Maintenance section;

(ii) the introduction of an 'abuse of a dominant position' clause similar to S. 46 of the Australian Trade Practices Act will replace our current monopolisation provisions;

(iii) no law directly relating to price discrimination;

(iv) a movement away from the examinable/approvable/prohibited trade practices structure used in the Commerce Act.

(2) The Abuse of a Dominant Position Clause

(a) Comparison with S. 46 of the Australian Trade Practices Act
1974. If these amendments are introduced, price discrimination will likely be caught under the "abuse of a dominant position" clause. This may substantially change the legal status of price discrimination.

It is remembered that the three substantive elements of the 'abuse of a dominant position' clause are:

(i) the person must be in a dominant position in a market,
(ii) he must use that market power,
(iii) to attain an anti-competitive purpose.

The proposed test differs slightly from the Australian test. The person must be in a "dominant position in a market", and not necessarily in a "position substantially to control a market", the latter being considered to require a higher level of control, and the person must "use that position" rather than "take advantage of that power", again the Australian test requiring a higher threshold.

It is debatable whether the lower threshold tests dramatically alter the effectiveness of the proposed test. As argued by Wilson\textsuperscript{23}, the Australian Commission has been easily satisfied that a firm has the requisite market power and has used that power. Probably the major significance of the lower threshold test is to indicate to our Commission and Courts that the section is intended to be effective and not remain unutilised like the current monopolisation provisions.

(b) Determining a Violation. A seller who is engaged in price discrimination should be considered to have sufficient market power to satisfy the "dominant position in a market" requirement. This also applies to the buyer who successfully induces a discriminatory discount. Alternatively, a structural test of "dominant position" may be used - if a firm has X % of the market, defined in terms of product market, geographic market and functional level. The first test is considered

\textsuperscript{23} Wilson, \textit{supra}, p. 285 n. 29 and accompanying text.
more appropriate because it more closely accords with the economic concept of market power as being able to affect prices and quantities at which the goods or services are sold.

It also seems that, as a seller requires market power before he can discriminate, then he must use that power in order to discriminate. But is this the proper meaning of 'use', or should 'use' be given a more action-orientated meaning? A seller engaged in predatory conduct may use monopoly profits and inter-area subsidization to finance his activities and a large buyer may use a threat to switch suppliers to induce a discrimination. These are legitimate cases where market power is used to discriminate in price or to induce a discrimination. But consider the seller forced to grant a discriminatory discount to a large buyer. Can it be said that he uses his market power to grant the discount?

Fortunately there is no need to decide this dilemma. The proposed abuse of a dominant position test is believed to contain a 'purpose' test. Generally the only forms of price discrimination undertaken for an anti-competitive purpose are the 'kill-the-rival' and the 'keep-them-in-line' forms. There is generally no question that a seller who engages in predatory activity to kill his rivals uses his market power to achieve his aims.

The typical 'hold-them-in-line' form of price discrimination is attacked by other means, such as combining the RPM and refusal to deal provisions. The Bailies case involved this form of price discrimination. Where a case is brought under the abuse of a dominant position section, the aggressive purpose of the discrimination should be sufficient to indicate that the seller used his dominant position. Therefore if the "dominant position" and "purpose" tests are satisfied, then the "use of that power" test will also be satisfied.
How will 'purpose' be determined? It seems unlikely that a narrow cost-based test such as the Areeda and Turner test will be adopted. The Commission has shown itself willing to discard unsubstantiated arguments of defendants and infer the true motive for an action from the circumstances surrounding the trade practice. Where the case has been appealed the inference has been accepted by the Appeal Authorities. Kempthorne Prosser\textsuperscript{24} and Bailies are examples of this willingness. The motive aspect of the Trade Practices Act 1958 and the Commerce Act 1975 is perhaps less important than under the "abuse of a dominant position" section and the new provisions may require a higher standard of proof, however, it is expected that the Commission will retain its current perceptive approach to this problem.

(c) **Comparison of the Current and Proposed Monopolisation Provisions.** As well as the possibility of a lower threshold test for monopoly, two other changes distinguish the current and proposed legislation. These are the use of the 'purpose' test and not an effect test, and the focus on competitors rather than general industry effects. The significance of the 'purpose' test is to confine application of the Section to cases of price discrimination where an anti-competitive motive can be discerned, such as the kill-the-rival and hold-them-in-line forms. Application of the section to most cases where there is secondary line injury would be prevented because discounts causing secondary line injury are generally not granted or induced for the purpose of destroying a competitor.

To understand the reason for this exclusion, one should reflect on the rationale for the purpose test. A monopolist, like any other market participant, desires to improve his competitive position and increase his long-term profits. This behaviour is acceptable, provided

\textsuperscript{24} In re Kempthorne Prosser & Co's New Zealand Drug Co. Ltd and Sharland & Co. Ltd., [1964] NZLR 49.
the monopolist achieves his goals through superior efficiency, technical knowledge, and consumer preference. Antitrust law is not concerned with monopoly, per se, but with the abuse of monopoly power to achieve anti-competitive goals. The purpose test distinguishes between acceptable behaviour and unacceptable behaviour (such as predatory pricing, foreclosing supplies or outlets to rivals, boycotts, etc) and allows the monopolist to pursue those acceptable goals yet prevents him pursuing anti-competitive goals.

It is not thought that the focus on competitors rather than competition will introduce the same deficiencies that resulted from the focus on competitors in Robinson-Patman cases. That Act uses an 'effect' and 'competitors' test, while the proposed section uses 'purpose' and 'competitors'. The distinction is important. The purpose test focusses on the behaviour of the monopolist. The 'effect' and 'competitors' combination focusses solely on the welfare of a single competitor. This approach is myopic and ignores whether the behaviour of the monopolist is acceptable and whether competition in general is impaired.

(d) Conclusion. The abuse of a dominant position section, as it might be enacted and applied in New Zealand, is suited to the problems of monopolistic abuse but has application to price discrimination only when it is instigated by a monopolist for the purpose of maintaining and extending a monopoly position. A section such as this should not be seen as adequate to prevent many forms of price discrimination resulting from the abuse of buying power.
CHAPTER VIII

CONCLUSIONS AND RECOMMENDATIONS

8.1 AN EVALUATION OF PRICE DISCRIMINATION LAW

(1) Introduction

This thesis has set out to answer two questions: whether price discrimination is undesirable; and, if so, whether it is possible to prevent such price discrimination.

An evaluation of price discrimination according to economic criteria reveals that it may have deleterious effects on competition if practiced systematically. The view that price discrimination may be undesirable is also supported by arguments that it is "unfair" and that it tends to harm small business to a greater extent than large business. These three arguments have motivated price discrimination legislation in many developed countries.

Despite these economic, ethical, and protectionist arguments, price discrimination legislation has been heavily criticised and there are many who call for the repeal of such legislation. The reason is that the second question must be answered in the negative: it is not possible to prevent undesirable price discrimination without causing unintended ill effects.

(2) Goals of Price Discrimination Law

When deciding whether to enact price discrimination law, the onus is first placed on those who support such law to show that it will achieve its desired goals. These goals are the prevention of predatory pricing; the prevention of monopoly in the distribution channels; and the promotion of equal opportunity and fairness and the protection of
small business. We have seen that price discrimination is either not necessary to, or not able to achieve these goals.

(a) **Price Discrimination and Predation.** We have noted that there is a dubious link between price discrimination and predation. Predation occurs where a monopolist uses his power to exclude a competitor. It is illogical and inconsistent to outlaw predation under price discrimination legislation. There are two problems: the predatory low price and the monopolistic high price. Treating predation and monopolisation as a problem of price discrimination shifts attention away from these problems and towards the link between the high and low prices.

We also do not consider that predation is a common or necessarily a logical practice among monopolists. We feel that there is little real danger that predatory pricing will lead to the growth of monopolies in New Zealand.

We consider that monopolisation provisions, properly enforced, would give sufficient protection against the predator. Any price discrimination statute would either duplicate (or be less effective) than the monopolisation provisions because it used the same injury test, or it would prevent desirable price discrimination (eg. promotional pricing, pricing to meet differing market conditions, etc) because it used a lower threshold injury test. Therefore we do not accept the need for, or the desirability of a price discrimination statute to prevent primary-line injury.

(b) **Monopoly in the Channels of Distribution.** Price discrimination does not significantly affect concentration levels at the distribution level. This is determined by more immediate factors, especially consumer preference for the services offered by small business, and the ability of small business to adopt more efficient methods of distribution such as co-operatives.
Even if concentration increased at the level of distribution, this does not imply that a monopoly or oligopoly exists. Vigorous competition between remaining firms and the ease of entry and exit to the market should provide the public with adequate protection from monopoly.

Again, we must conclude that price discrimination legislation is not necessary to prevent monopoly in the channels of distribution, and in fact may even add to concentration by inhibiting the development of new methods of distribution.

(c) Fairness and Small Business. The major appeal of price discrimination is that it seems to equalize competitive opportunities between firms, whether they are large or small. This leads to 'fairness' and promotes small business.

However, price discrimination law does not promote fairness. In many cases, it may actually inhibit efficiencies being passed on to buyers, prevent functional discounts, inhibit or altogether eliminate channels of distribution, force a one-price system, etc. These effects cannot be considered 'fair' or in the interests of small business.

Also, the ease of circumventing price discrimination law suggests that it could not achieve equal opportunity.

Nor should the antitrust laws be orientated towards fairness for the small business. This is not promised to the competitor. Of paramount importance is the promotion of efficiency and competition. These goals form the basis of our economy and the justification for government intervention, and cannot be attained in conjunction with the goals of 'fairness' and the promotion of small business.

(3) Effects of Price Discrimination Law

Price discrimination law has many undesirable effects. These result from conceptual deficiencies and cannot be remedied by a change
in the language of a statute, or more flexible judicial interpretation.

(a) **Determining a discrimination.** It is impossible to give a
definition of discrimination that is so flexible as to accurately
capture only economic discrimination yet so concrete as to have
practical application. Considerations of risk, cost, opportunity cost,
etc., will plague any price discrimination statute. Limitation of an Act
to goods, or to 'like' transactions provides only a partial solution.
Unless price discrimination law properly identifies economic
discrimination, its effect will be to encourage such discrimination
rather than prevent it.

(b) **Low Threshold Injury.** The second difficulty of price
discrimination law is that to effectively control discounts granted to
the large buyer, a low threshold injury test in necessary. And, if it is
to have greater application than monopolisation legislation, a low
primary line injury test is also required.

This would mean that due recognition is not given to the pro-
competitive effects of price discrimination. Promotional pricing,
pricing to meet market conditions, and price discrimination that leads
to the disintegration of an oligopolistic pricing structure may all be
condemned.

Price discrimination often occurs during a transition period from
one market structure to another, e.g. where price discrimination
witnesses the entry of a competitor to a market, or where a large buyer
destroy the rigid pricing structure at the sellers' level. Such price
discrimination is strongly pro-competitive and should be encouraged.
Unless the competitive injury test distinguishes between pro- and anti-
competitive price discrimination, the result of such legislation may be
to prevent both.

One solution might be to limit the application of price
discrimination law. This may be achieved by limiting private enforcement, limiting the penalties for discriminating in price, and confining enforcement by Government agencies to concentrated industries.

However, price discrimination yields its greatest benefits in concentrated industries for it is here that pro-competitive forces can have their greatest impact. Thus, we come to the inescapable conclusion that price discrimination law must prevent both pro- and anti-competitive price discrimination.

(c) **Constraints placed on pricing.** These effects mentioned place undesirable effects on the pricing decisions of sellers and buyers. Price discrimination legislation constrains natural pricing in response to market pressures. Both the buyer and the seller are restricted.

Prices must be set in accordance with the legislation. Cost-plus pricing must be used (with the unacceptable definition of cost), and pro-competitive price discrimination is eliminated. Such legislation is in direct conflict with the competition philosophy.

The seller is caught between the law and the large buyer; the large buyer is caught between the law and competitive pressures from rivals. Unless the buyer and seller are allowed to meet those pressures legally, they will invent new and inefficient means of distribution and pricing which accommodate both pressures.

(d) **Intra-industry price rigidity.** The meeting competition defence leads to inter-firm price matching. This, in conjunction with the uniform pricing, means that all firms will adopt a single price. There are very close similarities between this and government price regulation, the difference being that under price discrimination law the market participants set the price.

(e) **Low Enforcement Priority** Because price discrimination does not significantly contribute to concentration levels, it should be seen as a low priority for enforcement. Price discrimination legislation may
either remain ineffective because it is not enforced, or it may consume limited resources of the enforcement agency in return for minimum benefit. These resources would be better directed to the control of trade practices, mergers and monopolies where there is some significant injury to competition.

8.2 RECOMMENDATIONS FOR NEW ZEALAND

(1) Primary Line Injury and Predation

Our first recommendation is to separate primary and secondary line price discrimination and treating the former as a form of monopolisation. Our argument for this is simple. Price discrimination causing primary line injury is a form of predation. The presence of differential pricing or inter-area subsidization is of little consequence to the question of whether a monopolist is destroying his rivals. Such a form of price discrimination should therefore be treated like any other form of undesirable conduct of a monopolist - under the monopolisation provisions.

(2) Secondary Line Injury

The second recommendation is to avoid any form of secondary line price discrimination law. Price discrimination causing secondary line injury is also a problem of monopolisation, however, the injury is never sufficient for the practice by itself to evoke the monopolisation provisions and there is rarely any predatory motive. Therefore separate price discrimination provisions employing a low threshold injury test would be required.

However, we have seen that where it is easy to establish a violation of a price discrimination statute, price rigidity has prevailed. Another problem is the low enforcement priority that price
discrimination would receive.

To this end, two amendments are mooted. The first is to attach the 'Refusal to Supply' provisions to specific trade practices rather than leaving refusal to supply as an independent practice. The second relates to limiting the application of the monopolisation provisions. This may be done in two ways. It may be emphasized that there must be an effect on competition, or a test of intent may be introduced to allow price discrimination where the purpose is not to destroy competition.

(3) **Cases where Price Discrimination is Ancillary to the Main Trade Practice**

The third recommendation concerns delivered pricing systems. It is felt that these systems may facilitate collusion or anti-competitive practices in an industry. Although they are forms of price discrimination, the problems of dealing with them distinguish them significantly from other practices of price discrimination. The questions concern collusion, tacit or otherwise. These also should not be treated as forms of price discrimination, but rather as forms of horizontal agreement between competitors.

Where price discrimination is used to enforce another trade practice, it is this trade practice that should be the focus of attention. Thus, refusal to deal provisions should not be used to attack discriminatory pricing itself. To prevent this indirect method of control of price discrimination, we recommend that such provisions should not stand alone but be attached to the RPM, exclusive dealing, etc, provisions.

(4) **Price Discrimination Law, and C.E.R.**

A further point to be discussed is whether we should enact price discrimination law to remain consistent with Australia after the introduction of Closer Economic Relations (CER). Price discrimination
law might be supported because it subjects all firms to the same legal restrictions, and also because it may be used to break down barriers between the two countries in the same way that such law has been used in the EEC.

The arguments against enacting such law are simple. Consistency may be a desirable goal although it would seem, given the criticism of Section 49 of the Australian Trade Practices Act 1974 by the Swanson and Blunt Committees and by academics and lawyers, that consistency would be better attained if the Australian Government were to repeal Section 49. If the purpose is to break down trade barriers, some form of law might be considered, however, it should not be disguised as a price discrimination statute, but rather should directly address the problem.

(5) Motivating Forces Behind Price Discrimination Legislation

The final thought, and perhaps the most important thought is provided by Dr. Pengilley in his paper on Section 49 of the Australian Trade Practices Act:

Political effect is based on rhetoric and politicians are, by definition, expert rhetoricians. It is words rather than logic which generate action. In attempting to consider Section 49 in a dispassionate sense we should always remember that the cool insights of cerebral man, whilst perhaps indispensable to social progress, rarely control ultimate activities, even intellectual ones.

The enactment (or strengthening) of price discrimination law is a matter of rhetoric. The base-line justifying price discrimination law is that it prevents discrimination. Like any other form of discrimination it should be condemned.

However, price discrimination is not a form of personal discrimination which should be condemned. The issues of price discrimination are far removed from those of personal discrimination. Nevertheless the writer accepts the cynical view of Pengilley that the enactment of price discrimination could be matter of rhetoric rather
than logic - a question of discrimination. Evidence for this can be seen in the enactment of the Robinson-Patman Act, and the retention of the Australian S. 49. The importance placed on small business and on 'fairness' in New Zealand suggests that price discrimination law could be enacted here also and the decision based more on impassioned rhetoric that logical thought.
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APPENDIX I

The Robinson-Patman Act

Section 2 of the Robinson-Patman Act provides that –

2 (a) That 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 ..., 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 allowances for differences in the cost of manufacture, sale or delivery resulting from different methods or quantities in which such commodities are to such purchasers sold or delivered: Provided, however, ... 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 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) That it shall be unlawful for any person engaged in 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 on 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) That 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) That it shall be unlawful for any person to discriminate in favour 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 according to all purchasers on proportionally equal terms.

(f) That it shall be unlawful for any person engaged in commerce, in the course of such commerce, knowingly to induce or receive a discrimination which is prohibited by this section.

3. 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 discriminations to his knowledge against competitors of the purchaser, in that, any discount, 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.

4. Nothing in this Act shall prevent a cooperative association from returning to its members, producers, or consumers the whole, or any part of, the net earnings or surplus resulting from its trading operations, in proportion to their purchases or sales from, to, or through the association.

Approved, June 19, 1936.
APPENDIX II

Section 2 of the Clayton Act 1914

(2) 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, which 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, where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce: Provided, That nothing herein contained shall prevent discrimination in price between purchasers of commodities on account of differences in the grade, quality, or quantity of the commodity sold, or that makes only due allowance for differences in the cost of selling or transportation, or discrimination in price in the same or different communities made in good faith to meet competition: 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.
APPENDIX III

Proposals of the Neal Committee

a) That it shall be unlawful for any person in the course of commerce to discriminate, either directly or indirectly, in the exaction of consideration for the sale, lease, transfer or provision of any commodity or service where (i) the two or more transactions involved in the discrimination involve commodities or services of like grade and quality, (ii) such commodities or services are sold, leased, transferred or provided for use, consumption, or resale within the United States or any place under the jurisdiction of the United States, and (iii) the effect of the discrimination may be substantially to lessen competition or tend to create a monopoly in any line of commerce.

b) A discrimination shall be held to have the effect described in subsection (a) only where:
   (i) The recipient of the benefit of the discrimination is in competition with others not granted the same treatment, the discrimination is substantial in amount, and the discrimination is part of a pattern which systematically favors larger competitors over their smaller rivals; or
   (ii) The recipient of the benefit of the discrimination is in competition with others not granted the same treatment, the discrimination is substantial in amount, and the discrimination imminently threatens to eliminate from a line of commerce one or more competitors whose survival is significant to the maintenance of competition in that line of commerce; or
   (iii) The person granting the discrimination is in competition with others serving significantly more limited areas (territories or classes of customers which are relevant lines of commerce), the discrimination is restricted to one or more such limited areas (representing a small part of the total area served by the person granting the discrimination), the consideration exacted in such limited areas is less than the reasonably anticipated long-run average cost of serving those areas (including capital costs), and the discrimination imminently threatens to eliminate from such a limited area one or more competitors whose survival is significant to the maintenance of competition in that area.

Provided, however, that the survival of a competitor is not significant to the maintenance of competition where, in the line of commerce affected, the number of competitors remaining, or the ease with which new competitors may enter, indicates that effective competition will not be suppressed for an appreciable period of time.

(c) It shall be a defense to a charge of discrimination that the lesser exaction of consideration was made in good faith to meet an equally low exaction of a competitor. The defense shall be allowed even though the equally low exaction of the competitor is unlawful, except in a suit seeking prospective relief against all or substantially all of the competitors practicing the discrimination; in the latter event, a discrimination otherwise unlawful may not be justified as meeting an equally low exaction of a competitor if the latter's exaction is unlawful.
(d) It shall be a defense to a charge of discrimination that the lesser exaction of consideration makes an appropriate allowance for differences in the cost of manufacture, distribution, sale, or delivery resulting from the differing methods or quantities involved in the transactions in question. An allowance is appropriate where the difference in consideration does not substantially exceed the difference in cost; where the difference in consideration does not exceed a reasonable estimate of the difference in cost; or where the difference in consideration is the result of a reasonable system of classifying transaction which is based on characteristics affecting cost of manufacture, distribution, sale or delivery, under which differences in consideration between classes approximate differences in cost. If a system of classification is held to be unlawful, the court or agency so ruling should indicate either (i) that the seller's customers are so similar in pertinent characteristics that no system of classification would be valid, or (ii) that a system of classification described by the court or agency may properly be employed in lieu of the one held to be unlawful.

(e) It shall be a defense to a charge of discrimination that the lesser exaction of consideration was in response to changing conditions affecting the market for or the marketability of the commodities or services 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. A charge of discrimination also may be rebutted by proof that the lesser exaction of consideration was available, on reasonably practicable conditions, to the person or persons allegedly discriminated against.

(f) Nothing herein contained shall prevent any person from refusing to deal with any other person. Provided, however, that the offer to deal on discriminatory terms shall be treated as a completed transaction for the purpose of according relief under this section.

(g) That it shall be unlawful for any person knowingly to induce or receive a discrimination which is prohibited by this section.

(h) Section 5 of the Federal Trade Commission Act shall not be held to prohibit any discrimination in the exaction of consideration for the sale, lease, transfer or provision of commodities or services, or the receipt of any such discrimination.

(i) Any order issued to enforce this section shall remain in effect for a limited time, stipulated at the time or entry and reasonably related to the nature of the violation. In no case shall an order remain in effect more than five years after the date of issue.
APPENDIX IV

S.38 of the Competition bill to Amend the Canadian Combines Investigation Act.

38(1) No supplier of an article, in dealing with one of his customers in Canada, shall refuse such customer sale and delivery of the article at any locality at which the supplier makes delivery of the article to any other of his customers, on the same terms and conditions of sale and delivery that would be available to the first-mentioned customer if his place of business were located in that locality.

(2) No supplier of an article shall refuse to deal with a customer in Canada or a person seeking to become a customer of Canada by reason only that such customer or person insists on taking delivery of the article at a particular locality at which the supplier sells and delivers the article to other customers.

(3) Any person who violates this section is guilty of an indictable offense and is liable to imprisonment for two years.