

IN THE MATTER OF
SAMUEL STORES, INC.

COMPLAINT, OPINION, AND ORDER OF DISMISSAL IN REGARD TO THE ALLEGED
VIOLATION OF SEC. 5 OF AN ACT OF CONGRESS APPROVED SEPT. 26, 1914

Docket 3210. Complaint, Aug. 21, 1937—Decision, Sept. 2, 1938

UNFAIR METHODS OF COMPETITION—"FREE GOODS" MERCHANDISING—IN GENERAL

The lawfulness, in connection with a merchandising plan, of "free goods" offers, recognized as powerful psychological magnets to draw trade and source from which merchant expects to benefit, either through immediate direct profit on some other article which must be purchased, or indirectly through increased good will and future patronage, depends on the terms of the offer and the underlying and surrounding facts, and the real test, except where the practice is employed by large concerns to eliminate weaker competitors, is whether there is a deception of the purchaser or use of a lottery method or chance device in distribution of such goods, in which event transaction would fall within purview of *Federal Trade Commission v. Keppel & Bro.*, 291 U. S. 304.

UNFAIR METHODS OF COMPETITION—"FREE GOODS" MERCHANDISING—PURCHASER
DECEPTION—GOODS' COST—CONDITIONAL PURCHASE MERCHANDISE—WHERE LIM-
ITED SACRIFICE NORMAL PROFIT IN OFFER AND SALE

Where the merchant, to attract new customers, sacrifices, for a limited period of time, portion of his normal profit on his entire line, he may receive no immediate direct profit from the transaction, and merchandise required to be purchased must bear not only its own cost and its own share of the general operating overhead, but also cost of the "free goods" and said goods' overhead share, in which event "free goods" offer is hardly deceptive, since purchaser actually does obtain specified "free goods" at no additional cost over the ordinary and regular price of the merchandise required to be purchased, and, therefore, actually receives such goods without cost; the practice in such a case, in reality, being a convenient and impelling method of calling public attention to price reductions in goods which must be purchased.

UNFAIR METHODS OF COMPETITION—"FREE GOODS" MERCHANDISING—PURCHASER
DECEPTION—GOODS' COST—CONDITIONAL PURCHASE MERCHANDISE—WHERE COST
RECOUPMENT BY PREJUDICIAL CHANGE IN PRICE OR QUALITY OF

Purchaser has right to believe that merchant will not directly and immediately recover, in whole or in part, cost of the "free goods" by marking up price of article which must be purchased or substitution of inferior merchandise, and where merchant recovers any portion of cost of such "free goods" directly from the immediate transaction through use of such methods, there is necessarily deception of purchaser, since so-called "free goods" are not in any sense free. *Standard Education Society v. Federal Trade Commission*, 302 U. S. 112, 116.

UNFAIR METHODS OF COMPETITION—"FREE GOODS" MERCHANDISING—PURCHASER DECEPTION—CONDITIONAL PREREQUISITES—INITIAL AND FULL DISCLOSURE OBLIGATION OF MERCHANT

"Free goods" offers conditioned upon purchase of other merchandise or upon performance of a service sometimes appear, at first impression, to be unconditional, through prominently featuring offer in such way as to obstruct or minimize condition attached thereto, with resulting deception of purchaser, at least in initial or "contact advertising" stages, and it is not sufficient that purchaser be made fully aware of any conditions before transaction is finally consummated, but he must be fully apprised of all the terms and conditions of the offer at its inception in order for there to be an assurance that no deception is involved in transaction, later full explanation not sufficing to correct vice of initial deception. *Standard Education Society v. Federal Trade Commission*, 302 U. S. 112, 115, 116; *Holland Furnace Co. v. New Holland Machine Co.*, 24 F. (2d) 751, 753; *Fairyfoot Products Co. v. Federal Trade Commission*, 80 F. (2d) 684, 687.

UNFAIR METHODS OF COMPETITION—"FREE GOODS" MERCHANDISING—PURCHASER DECEPTION—CONDITIONAL PURCHASE MERCHANDISE—WHERE FULL INITIAL DISCLOSURE, ABSENT ELEMENT OF MONOPOLY, LOTTERY, FICTITIOUS PRICE MARKING, SUBSTITUTION OR OTHER DECEPTION

Where, on complaint charging corporation engaged in interstate sale and distribution of wearing apparel and other merchandise, and in operation of a chain of 30 or more stores, with practice of an unfair method of competition through use of such false and misleading pretended "free goods" offers in advertising as " * * * Sensational 2-day Get-Acquainted Gift Offer! Free! For ladies. For men. Free! All-weather sport coat with any purchase of \$25.00 during Grand Opening Sale! * * *," and "FREE! Choice of \$6.95 dress or men's shoes With any \$25.00 purchase!," in that, as alleged, cost of supposed "free goods" was covered in price of conditional merchandise involved, and said goods were, therefore, "not in any sense a gift or gratuity given to customers without cost to them," it appeared that cost of said goods was charged to advertising budget of said corporation, and became part of its general operating overhead, terms and conditions were clearly and conspicuously stated, such goods were actually given to all purchasers making required purchase and in specified amount, customers were not restricted or limited, and prices of all merchandise sold prior to and after such "free goods" period were based on standard mark-up and were the same, merchant did not occupy monopolistic or near-monopolistic position, and deception was not present through substitution of inferior merchandise or otherwise:

Held, That corporation in question fulfilled terms of its "free goods" offer by actually furnishing to every customer making any purchase in specified sum specific article offered as "free goods," and that offer did not, under circumstances involved, constitute unfair method of competition, and complaint dismissed.

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Before *Mr. John W. Norwood*, trial examiner.
Mr. Carrel F. Rhodes for the Commission.
Katz & Sommerich, of New York City, for respondent.

COMPLAINT

Pursuant to the provisions of an Act of Congress, approved September 26, 1914, entitled "An Act to create a Federal Trade Commission, to define its powers and duties, and for other purposes," the Federal Trade Commission, having reason to believe that Samuel Stores, Inc., a corporation, hereinafter referred to as respondent, has been for more than 1 year last past and is now using unfair methods of competition in commerce, as "commerce" is defined in said act of Congress, and it appearing to the Commission that a proceeding by it in respect thereof would be to the public interest, hereby issues its complaint stating its charges in that respect as follows:

PARAGRAPH 1. Respondent, Samuel Stores, Inc., is a corporation organized and existing under and by virtue of the laws of the State of New York, with its principal office and place of business located at 460 Fourth Avenue, New York City, N. Y. Respondent is now, and for more than 1 year last past has been, engaged in the business of manufacturing, advertising, selling, and distributing men's clothing and women's apparel and other articles. It now causes, and for more than 1 year last past has caused, its said products when manufactured to be shipped from its principal place of business in New York City, in said State, through and into the several States of the United States other than the State of origin, where said products are delivered to retail stores owned and operated by respondent.

Respondent, in the course and conduct of its said business, advertises and sells its said products to the consuming public through a chain of 30 or more retail stores owned and operated by it throughout the East and Middle West and in the District of Columbia. Among the retail stores so owned and operated by respondent is one located at 731 Seventh Street N. W., Washington, D. C., known and designated as "Long's" or "Long's Credit Clothing."

Respondent's method of sales is through advertisements and sales talks whereby it holds out to the public as an inducement to buy its merchandise an offer to give to each purchaser of \$25 of said merchandise "Free" and without cost, the "Choice of a \$6.95 dress or men's shoes," a "Ladies' or men's all-weather sport coat," or other merchandise.

Respondent is now, and for more than 1 year last past has been, in substantial competition with other corporations and with persons,

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firms, and partnerships engaged in the sale of men's clothing, women's wearing apparel, and other articles similar to those sold by respondent in commerce between and among the various States of the United States and in the District of Columbia.

PAR. 2. In the course and conduct of its said business as described in paragraph 1 hereof, in soliciting the sale of and selling its said products, respondent now represents, and for more than 1 year last past has represented, in newspapers, magazines, pamphlets, circulars, letters, radio broadcasts, and other forms of advertising media having an interstate circulation, and in sales talks and on signs posted around its retail stores located in the several States of the United States and in the District of Columbia, as follows:

GRAND OPENING TODAY!

The Stage is Set—Today the curtain rises on the brilliant new Long's Credit Store!! Sensational 2-day Get-Acquainted Gift Offer! Free! For ladies. For men. Free! All-weather sport coat with any purchase of \$25.00 during Grand Opening Sale! Leave your Cash at Home!

FREE! Choice of \$6.95 dress or men's shoes with any \$25.00 purchase!

PAR. 3. In truth and in fact the cost of the "\$6.95 dress or men's shoes" and "Ladies' or men's all-weather sport coat," or other merchandise, offered to be given "Free" to the purchaser by respondent with each purchase of \$25 of said merchandise, bought as described in paragraph 2 hereof, is included in the said \$25 paid for the merchandise purchased; and said so-called "Free" goods are not in any sense a gift or gratuity given to customers without cost to them.

PAR. 4. The representations of respondent as aforesaid are false and misleading and have had and do have a tendency and capacity to mislead and deceive members of the purchasing public into the mistaken and erroneous belief that upon making purchases of specified amounts of respondent's merchandise the articles advertised as "Gifts" will be received unconditionally and without cost, when such is not true in fact. The said representations of respondent have had and do have the capacity and tendency to induce members of the purchasing public to buy respondent's merchandise because of the erroneous beliefs engendered by said false and misleading representations, and to divert trade unfairly from competitors of respondent engaged in the sale of men's clothes and women's apparel and like merchandise similar to that sold by respondent in commerce in and among the various States of the United States and in the District of Columbia. Said acts and practices deceive the public and injure competitors who

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do not misrepresent the conditions or terms upon which said sales are made.

PAR. 5. The above alleged acts and practices of respondent are all to the prejudice and injury of the public and of respondent's competitors and constitute unfair methods of competition in commerce within the intent and meaning of Section 5 of an Act of Congress, approved September 26, 1914, entitled "An Act to create a Federal Trade Commission, to define its powers and duties, and for other purposes."

OPINION

Acting pursuant to the authority of the Federal Trade Commission Act, the Commission issued its complaint charging the respondent with the use of unfair methods of competition through the use of "free goods" advertising as a part of its merchandising plan. The respondent answered that the "free goods" referred to in its advertising were actually furnished to the purchasers of its other merchandise in conformity with its advertisements. The question in this case is whether, under all the circumstances, the offering of the so-called "free goods," which was conditioned upon the purchase of other merchandise, is an unfair method of competition.

Respondent is engaged in the interstate sale and distribution of wearing apparel and other merchandise. It operates a chain of 30 or more stores, and in the operation of its business it is in competition with competitors selling similar merchandise in interstate commerce.

Through various advertising media the respondent represented that for a limited time it would give certain specified merchandise free with the purchase of any other merchandise in a specified amount. The evidence shows the cost of the articles designated as "free" and which were given in connection with the purchase of other merchandise in a specified sum was charged to respondent's advertising budget and became a part of the general operating overhead of the business. The advertisements used by the respondent clearly and conspicuously stated the terms and conditions under which the so-called "free goods" could be obtained by customers. The "free goods" were actually given to all purchasers who made the required purchase in the specified amount, thereby fulfilling the conditions upon which the gift was predicated. The customers were not in any way restricted or limited as to the articles of merchandise bought in making the purchase required in order for the customer to be eligible for the "free goods." The prices of all merchandise sold during the time when such "free goods" advertising was being carried on were based on a standardized mark-up and were the same both before and after the periods during which the

special offer was in effect, and the respondent fulfilled the terms of its "free goods" offer by actually furnishing to each customer making any purchase in a specified sum the specific article offered as "free goods."

The lawfulness of an offer of "free goods" in connection with a merchandising plan depends on the terms of the offer and the underlying and surrounding facts.

"Free goods" offers are recognized as powerful psychological magnets to draw trade and undoubtedly the merchant expects to benefit thereby, either through an immediate direct profit on some other article which must be purchased or indirectly through increased goodwill and future patronage.

Where the merchant, for the purpose of attracting new customers, sacrifices, for a limited period of time, a portion of his normal profit on his entire line, he may receive no immediate direct profit from the transaction. In fact, the merchandise required to be purchased must bear not only its own cost and its own share of the general operating overhead, but also the cost of the "free goods" and its share of the overhead. Under such circumstances, the "free goods" offer is hardly deceptive, for the purchaser actually does obtain the specified "free goods" at no additional cost over the ordinary and regular price of the merchandise required to be purchased. As far as the purchaser is concerned, therefore, he actually receives the "free goods" without cost. In reality the practice in such a case is a convenient and impelling method of calling attention of the public to price reductions in the goods which must be purchased.

There are, however, many conditional "free goods" offers which result in deception of the purchaser. In some instances, the merchant will increase the advertised price of the article required to be purchased over the ordinary and customary selling price in an amount sufficient to offset, in whole or in part, the cost of the "free goods." In other cases, the merchant will substitute inferior merchandise for that ordinarily and customarily sold at the designated price involved in the transaction, thus recovering, in whole or in part, the cost of the "free goods." In cases of this type the purchaser has a right to believe that the merchant will not directly and immediately recover, in whole or in part, the cost of the "free goods" by the marking up of the price of an article which must be purchased or substitution of inferior merchandise. If a merchant recovers any portion of the cost of the "free goods" directly from the immediate transaction through the use of such methods, there is necessarily a deception of the purchaser, for the so-called "free goods" are not in any sense free. The recent decision

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of the Supreme Court in the *Standard Education Society* case (302 U. S. 112, 116) indicates no sympathy whatever for such practices:

The practice of promising free books where no free books were intended to be given, and the practice of deceiving unwary purchasers into the false belief that loose-leaf supplements alone sell for \$69.50, when in reality both books and supplement regularly sell for \$69.50, are practices contrary to decent business standards. *To fail to prohibit such evil would be to elevate deception in business and to give to it the standing and dignity of truth.* (Italics supplied.)

Other offers of "free goods" conditioned upon the purchase of other merchandise or upon the performance of a service sometimes appear, at first impression, to be unconditional offers of "free goods." This is brought about by prominently featuring the "free goods" offer in such a way as to obscure or minimize the condition attached thereto, with a resulting deception of the purchaser, at least in the initial or "contact advertising" stages. It is not sufficient that the purchaser be made fully aware of any conditions before the transaction is finally consummated. He should be fully apprised of all of the terms and conditions of the offer at its very inception, in order for there to be an assurance that no deception is involved in the transaction. Any deception of the purchaser, whether occurring during the initial stages of the transaction, that is, in the advertisement first attracting the customer's attention to the "free goods" offer, or at any other stage of the transaction, is sufficient to render unlawful any so-called "free goods" offer, even though all terms and conditions may be later fully explained. *Standard Education Society v. F. T. C.*, 302 U. S. 112, 115-116; *Holland Furnace Co. v. New Holland Machine Co.*, 24 F. (2d), 751, 753; *Fairyfoot Products Co. v. F. T. C.*, 80 F. (2d), 684, 687.

In the event the nature of the goods to be given or the manner of distribution thereof depend in any way on chance, the transaction would be in the nature of a lottery and within the purview of the case of *F. T. C. v. Keppel & Bro.*, 291 U. S. 304.

The real test, except where the practice is employed by large concerns to eliminate weaker competitors, is whether there is a deception of the purchaser or use of a lottery method or chance device in the distribution of the "free goods." Where, as in this case, advertisements offering the "free goods" clearly and conspicuously state the terms and conditions under which the "free goods" may be secured, the merchant does not occupy a monopolistic or near-monopolistic position, the "free goods" are not distributed by lot or chance, and there is no deception through fictitious price marking of the goods sold, or through substitution of inferior merchandise, or otherwise, the "free goods" offer does not constitute in the opinion of the Commission, an unfair method of competition, and the complaint is accordingly dismissed.

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Order

ORDER OF DISMISSAL

This matter coming on to be heard by the Commission upon the complaint of the Commission, the answer of respondent, the testimony taken in support of the allegations of the complaint and in opposition thereto, and the briefs and oral arguments of counsel for the Commission and for the respondent, and the Commission being now fully advised in the premises.

It is ordered, That the complaint herein be, and the same hereby is, dismissed for the reasons set forth in the written opinion of the Commission filed simultaneously herewith.

IN THE MATTER OF
GOTHAM SALES COMPANY, INC., ET AL.

COMPLAINT, FINDINGS, AND ORDER IN REGARD TO THE ALLEGED VIOLATION
OF SEC. 5 OF AN ACT OF CONGRESS APPROVED SEPT. 26, 1914

Docket 3120. Complaint, Apr. 30, 1937—Decision, Sept. 3, 1938

Where a corporation and five individuals, officers, directing heads and sole stockholders thereof, engaged as wholesale dealers in a variety of peddlers' and retailers' supplies, including cosmetics, perfumes, dental, and shaving creams, toilet accessories, spices, extracts, and similar household notions, and in sale and distribution thereof in commerce among the various States and in the District of Columbia, in substantial competition with others engaged in sale and distribution of similar products in commerce as aforesaid, and including manufacturers, sellers, and distributors of like and similar products who refrain from advertising or representing, through their catalogs and other advertising media, that their merchandise has a merit, origin, or value which it does not have, or falsely that they are manufacturers; in advertising their said commodities through catalogs, price lists, and other printed matter published, issued and circulated through the mails to their customers and prospective customers in the various States and in said District—

- (a) Represented, through fictitious pricing and other means, that their products were customarily and regularly sold at prices greatly in excess of those for which they were actually ordinarily and customarily offered and sold to ultimate purchasers, and greatly in excess of the true and actual retail value thereof, and that their dental and shaving creams were put up in "Giant" sizes, and to dealer customers that they could make introductory combination offers to the public of "Free" goods in connection with merchandise sold them by said corporation and individuals, facts being it was not contemplated or intended that products in question would be sold for fictitious prices represented, but said prices were thus advertised and held out as customary and regular in order to place in hands of retailers means and instrumentality whereby purchasing public might be deceived and misled into belief that it was buying merchandise at price lower than that at which it was ordinarily sold, aforesaid creams were not put up in sizes known to trade and purchasing public as "Giant" sizes, but in same sizes in which similar products were ordinarily packed by competitors who do not thus describe the same, and products thus represented as "Giant 50¢ size" did not have any such resale value or price or usually and customarily sell for any such sum, and sale price of supposed "free" articles was covered in that paid for others included in particular deal;
- (b) Represented, through such designations as "Dr. Ross—Dental Creams" and "Dr. Sach's—Dental Creams," that products in question were made under formula perfected by member of medical or dental profession and made under supervision and direction of a doctor and that they had, as a result thereof, superior or special qualities, and through use of such words as "Odeurs de Paris," "Perfumes of France," "Parfums de Paris," in referring in catalogs and other advertising literature to perfumes sold by them, and