

after service upon them of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which they have complied with the order to cease and desist.

IN THE MATTER OF
FEDERAL EMPLOYEES' DISTRIBUTING COMPANY, INC.,
ET AL.

ORDER, ETC., IN REGARD TO THE ALLEGED VIOLATION OF THE
FEDERAL TRADE COMMISSION ACT

Docket 7289. Complaint, Nov. 5, 1958—Decision, Nov. 23, 1959

Order dismissing, for failure to sustain the charges, complaint charging a Los Angeles five-store buying service with representing falsely that it was a non-profit corporation affiliated with the Federal Government, that membership was limited to Government employees, and that only members who had paid a \$2 fee could make purchases; that all profits were passed on to its purchasing members; and that the retail price of its merchandise was cost plus 5%.

Mr. Eugene Kaplan for the Commission.

Mr. Edward L. Butterworth of *Butterworth & Smith*, of Los Angeles, Calif., for respondents.

INITIAL DECISION BY LOREN H. LAUGHLIN, HEARING EXAMINER

This proceeding is one brought under the provisions of the Federal Trade Commission Act, the complaint charging in substance that by reason of false advertisements relating to the nature and operations of respondent corporation and its business the public are misled and the respondents are, therefore, guilty of unfair and deceptive acts and practices and unfair methods of competition in commerce. The respondents deny having made any false, misleading, and deceptive representations and further deny that they have maintained a substantial course of trade in commerce and pray dismissal of the complaint. The charges will be hereinafter recited in detail, and the evidence pertaining thereto fully analyzed and discussed.

In this initial decision the hearing examiner dismisses the complaint and proceeding for reasons hereinafter more fully set forth.

The complaint herein was issued November 5, 1958, and was there-

after duly served upon respondents, who, after certain preliminary motions had been disposed of, filed answer on February 26, 1959. A formal prehearing conference was held in Los Angeles, California, on February 18, 1959, as a result of which the time required for the hearing of the case was substantially curtailed. Hearings on the case-in-chief and the defense were also held in Los Angeles from March 2 to 4, 1959, inclusive. Upon the Commission's case having been rested, several motions to dismiss were made on behalf of respondent corporation and its officers, which motions were denied by the hearing examiner without prejudice to their renewal at the close of all the evidence (R. 205-213). The respondents thereupon proceeded with their defense, after which both parties rested (R. 348). The parties in due course filed their respective proposed findings of fact, conclusions of law, and orders, and the case was orally argued at length in Washington, D.C., on July 28, 1959, and final submission taken. The record is comparatively short, consisting of some 468 pages including over 100 pages of oral argument. The evidence itself consists of the testimony of an attorney-examiner of the Commission, the respondents Bishop and MacFarlane, officers of respondent corporation, and one G. F. Von Mueffling, its general manager. Documentary evidence consists of eleven exhibits of the Commission and 71 exhibits of the respondents pertaining to incorporation, business operations and the advertising questioned therein. The case was ably tried, briefed, and argued by the respective counsel and all issues necessary for determination fully presented. The proposals of the parties insofar as adopted are set forth herein, and all others have been rejected.

There is very little substantial dispute in this case as regards the evidence, although the contentions of the parties as to the nature and effect of the evidence are in direct contradiction. The burden of proof under Section 7(c) of the Administrative Procedure Act and Section 3.14(a) of the Commission's Rules of Practice for Adjudicative Proceedings rests upon counsel supporting the complaint, and as hereinafter more specifically found he has failed to maintain this burden with regard to the charges of false, misleading, and deceptive advertising, which are the gist of the complaint. It is found, however, that the Commission has jurisdiction of the subject matter of the complaint.

Respondents have raised the question of the Commission's jurisdiction on the premise that there is no substantial evidence upon which it can be found that the respondent corporation was engaged in interstate commerce. Since this question must be disposed of adversely to respondents, it will be decided before passing to the

merits of the case although reference will be made to certain factual findings which are more specifically referred to in the subsequent findings on the merits.

The complaint charges, in substance, that the respondent corporation, among other things, solicited memberships and also transmitted other advertising matter through the United States mails to members of the public located not only in California but in a nine-Western State area; that they also received payment for and distributed their membership cards by such mails and shipped certain commodities handled by said corporation from the State of California to purchasers thereof in other states and territories in a substantial volume of business in commerce. It is further charged that the merchandise offered for sale by respondents throughout their said business operations "are all commodities commonly sold, but not limited to, items normally offered for sale and sold in department stores, such as men's and women's wearing apparel, household goods and appliances, drugs, cosmetics, etc." Respondents admitted all of said matters except the alleged substantiality of their business in commerce and that they deal in "drugs." The further allegations as to the five alleged false, misleading and deceptive advertising practices of respondent corporation in interstate commerce state cause for complaint under both §§5 and 12 of the Federal Trade Commission Act and if such allegations were supported by the evidence, such findings would require the issuance of an order against respondents herein.

The Commission, of course, is a body of limited jurisdiction and in a certain limited sense a failure of proof on the merits might be considered to be failure of jurisdiction. But it is basic that the jurisdiction of a tribunal is not confined to deciding matters correctly (*State of Iowa v. F.P.C.* (C.A. 8, 1950), 178 F. 2d 421, 428, and *Coates v. C.I.R.* (C. A. 8, 1956), 234 F. 2d 459, 463). A court or agency is not confined to one set of standards and principles of judgment if it acts within the jurisdiction conferred upon it (*Pyramid Moving Co. v. U.S.* (D.C., N.D. Ohio, E. Div. 1943), 57 F.S. 278, affirmed 322 U.S. 714 (1944), rehearing denied 323 U.S. 811 (1944)). The power to hear and decide is what constitutes jurisdiction. Error in the decision which is rendered, while ground for an appeal, is not a failure of jurisdiction.

In the proceeding at bar the complaint alleges a cause of action under §5 of the Federal Trade Commission Act. With respect to the substantiality of the interstate business done, respondent claims, and with justification on the record, that the amount of sales made in interstate commerce are not proved with certainty. This is prem-

ised upon the testimony of the Commission's attorney-examiner Marita Kellum, who investigated the case, the testimony of corporate respondent's manager Von Mueffling, and a stipulation of record, which comprise the entire evidence pertaining to the volume of such interstate business. Miss Kellum testified without contradiction, in substance, that respondent Bishop told her in the course of her investigation that the mail order business done by respondents was "about one percent" of the total sales of corporate respondent (R. 146-147). Commission's Exhibit No. 6, a stipulation executed by respondents, stated that its annual gross sales in 1957 and 1958 were in the respective amounts of \$27 million and \$30 million. Upon this evidence, counsel supporting the complaint has urged that about one percent of respondents' gross sales in 1958 would be about \$300,000, which is, of course, a very substantial amount of business. But respondents contend that the testimony of Von Mueffling was to the effect that their sales outside the State of California were "an infinitesimal amount," "a very minor fraction of one percent" (R. 116). This speculative and uncertain evidence does not sustain a finding that sales made to people residing outside of the State of California were substantial. This, however, does not preclude the attachment of the Commission's jurisdiction. Von Mueffling also testified that some 7,000 to 9,000 copies of *The Fedco Reporter* were mailed out of the State of California each month (R. 117). This magazine, the evidence discloses, is substantially the only form of advertising that respondent corporation employs. Advertising is an integral part of a concern's business of production and distribution (*Ford Motor Co. v. F.T.C.* (C.C.A. 6, 1941), 120 F. 2d 175, cert. denied (1941), 314 U.S. 668; and *General Motors Corp. v. F.T.C.* (C.C.A. 2, 1940), 114 F. 2d 33, cert. denied, 312 U.S. 682); advertisements in commerce cannot be separated from the sale of goods and are themselves a part of interstate commerce, *Progress Tailoring Co. v. F.T.C.* (C.C.A. 7, 1946; 153 F. 2d 103); and interstate communication by newspapers as interstate commerce, (*Associated Press v. U.S.* (1937), 301 U.S. 103, 128-129).

In any view of the case the transmittal of some 7,000 to 9,000 magazines monthly which are chiefly advertising matter to members outside of the State of California who are prospective purchasers of respondents' merchandise is a substantial amount of interstate advertising regularly disseminated by mail and whether local sales are made in California (*Darr v. Mutual Life Insurance Co.* (D.C. S.D., N.Y., 1947), 74 F.S. 80, 84) or not made at all (*Jaffe v. F.T.C.* (C.C.A. 7, 1943), 139 F. 2d 112) is immaterial since the business as a whole constitutes interstate commerce.

Furthermore, in this proceeding the complaint alleges a cause of action under §12 of the Federal Trade Commission Act inasmuch as it clearly charges that respondent corporation, among other things, sells drugs and cosmetics. The evidence sustains such charges. The Fedco Reporter advertising such products is mailed monthly to 360,000 members. Respondents do not dispute the sale of cosmetics although they deny they sell drugs. Nevertheless, they have advertised drugs for sale. See Commission's Exhibit 2, p. 23, and the following exhibits of respondents: 39, p. 9; 62, p. 5; 63, p. 13; 64, pp. 5 and 13; 65, p. 15; 66, pp. 6, 10, and 14, and 69, p. 29, where vitamin tablets are advertised for sale. Vitamins are either a drug or a food under §15 (b) or (c) of the Act. See *F.T.C. v. National Health Aids, Inc., et al.* (D.C., Md. 1952), 108 F.S. 340, 345, and order granting temporary injunction, November 13, 1952, reported at F.T.C. Statutes and Decisions, 1949-1955, at pp. 780-784; and 49 FTC 601.

The respondents' said monthly magazine also advertises various foods and drinks which come under the definition of food in §15(b) of the Federal Trade Commission Act, such as candy, meats, liquor, nuts, fruit, and cheese. See Commission's Exhibits 1, pp. 5 and 25; and 2, pp. 2 and 15; and the following exhibits of respondents: 59, pp. 13, 26, and 32; 61, p. 10; 62, p. 11; 63, pp. 3 and 10; 64, p. 16; 65, p. 16; 66, p. 5; 68, pp. 13 and 26; 69, p. 31; 70, pp. 13 and 21; and 71, p. 2. Respondents also advertised cosmetics within the terms of §15(e) of the Act. See Commission's Exhibit 1, p. 5, and Respondents' Exhibit 69, p. 29. Respondents admit selling such latter products. While the advertisement of articles of food is not specifically alleged, it doubtless is included under the "etc." in the allegation of the complaint above referred to. It is probably unnecessary to determine specifically whether the extensive advertisements by respondents in their said monthly magazine of optical goods and services and hearing aids are devices under §15(d) of the Act, although within the said alleged "etc." they undoubtedly are such. Respondents also advertised furs extensively but that is immaterial here since this proceeding is not brought under the Fur Act. It cannot be urged that none of these advertisements misrepresented the quality or character of the goods so advertised because under §12 of the Act it is not necessary that an advertisement to be false relate to such matters. It is sufficient if any false advertisement is transmitted either by the U.S. mails or in commerce by any means "for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase of food, drugs, devices or cosmetics." Respondents' advertisements certainly do this. In H.R.

No. 1613, 75th Congress, August 19, 1937, it was said with reference to this definition:

The definition is broad enough to cover every form of advertisement deception over which it would be humanly practicable to exercise governmental control. It covers every case of imposition on a purchaser for which there could be a practical remedy.

See *FTC v. Thomsen-King & Co., Inc.* (D.C.N.D., Ill., 1940), reported in Statutes and Decisions, FTC, 1939-1943, pp. 658-662, supersedes as denied C.C.A. 7, 1940, 109 F. 2d 516. In *F.T.C. v. National Health Aids, Inc.*, *supra*, the injunction granted was premised against distribution of cosmetics, not because there was any false representation as to their composition or quality but because they were advertised by U.S. mails or in commerce otherwise under a prize puzzle contest which amounted to a gambling transaction. See also *F.T.C. v. Winship Corp., et al.* (D.C.S.D., Iowa, 1940), reported in Statutes and Decisions, FTC, 1939-1943, pp. 663-666. It is now well-established that the Commission has jurisdiction over advertising by mail in the case of such products whether or not any sale has been made if the advertising was false in any particular. See *Shafe v. F.T.C.* (C.A. 6, 1958), 256 F. 2d 661, 664; *Mueller v. U.S.* (C.A. 5, 1958), 262 F. 2d 443, 446-447; and *Wybrant System Products v. F.T.C.* (C.A. 2, 1959), 266 F. 2d 571, 572; also *Gilbert S. Bishop, et al.*, FTC Docket No. 6554.

It is, therefore, manifest that the Commission has jurisdiction in the present proceeding under either §§5 or 12 of the Federal Trade Commission Act or under both sections. The respondents did not raise the question of whether respondent corporation was one of a type included under the definition of "corporation" in §4 of the Act but, inasmuch as jurisdiction over the subject matter cannot be conferred, that question has been fully explored by the hearing examiner and will be discussed in a subsequent portion of this decision which relates to the charge that the corporate respondent has falsely advertised itself as a non-profit corporation as charged in paragraph 4(d) of the complaint.

Counsel supporting the complaint called no consumer witnesses to testify concerning their dealings with the respondents or their reliance upon an interpretation of respondents' advertising. He was not required to do so. See *Zenith Radio Corp. v. F.T.C.* (C.C.A. 7, 1944), 143 F. 2d 29, 31, and *New American Library, etc. v. F.T.C.* (C.A. 2, 1954), 213 F. 2d 143, 145. It is clear from his proposals and oral argument that he desires such matters determined by the hearing examiner in the first instance as a matter of expertise.

Since it is conceded on the record that the respondents at the time of trial had approximately 360,000 regular and associate members, most of whom resided in the Los Angeles area or elsewhere in southern California not far from the place where the hearing was held, had there been complaining members of respondent corporation, their testimony would have been readily available. When Miss Kellum investigated the case, the membership rolls were open to her, and at that time there were about 270,000 (R. Ex. 22, p. 2, Nov. 23, 1957).

But in the absence of the testimony of any consumer witnesses as to the meaning or effect of the advertisements in the record which are indisputably those of respondent corporation, the hearing examiner must determine from his experience in dealing with such matters "the natural and probable result of the use of advertising expressions" contained in the challenged advertising. See *E. F. Drew & Co., Inc. v. F.T.C.* (C.A. 7, 1956), 235 F. 2d 735, 741. In the opinion of the examiner, if he possesses expertness in this field it is from his experience as indicated in the *Drew* case, *supra*. Experience in the interpretation of advertising by the Commission or its examiners arises from frequent dealing with that particular subject just as a domestic relations judge becomes familiar with the problems arising out of divorce cases or a criminal judge becomes familiar with the various types of evidence and trial tactics met with in such causes. Expertness does not imply the right to assume non-existent facts or to make unreasonable and unfair inferences. It is now well-established that in federal administrative law, "an administrative agency with power after hearings to determine on the evidence in adversary proceedings whether violations of statutory commands have occurred may infer within the limits of the inquiry from the proven facts such conclusions as reasonably may be based upon the facts proven." See *Republic Aviation Corp. v. N.L.R.B.*, 324 U.S. 793, as quoted and followed in *Radio Officers v. N.L.R.B.* (1954), 347 U.S. 17, 48-49. See also *F.T.C. v. Pacific States Paper & Trade Assn.* (1927) 273 U.S. 52; *Brown Fence & Wire Co. v. F.T.C.* (C.C.A. 6, 1933), 64 F. 2d 934; *E. F. Drew & Co., Inc. v. F.T.C.*, *supra*. The doctrine of expertise is not a mysterious grant of unusual authority to the Commission or its examiners, but as the Court said in *Radio Officers v. Labor Board*, *supra*, at page 49, it had but restated,

* * * a rule familiar to the law and followed by all fact-finding tribunals—that it is permissible to draw on experience in factual inquiries * * * [50] (A) fact-finding body must have some power to decide which inference to draw and which to reject * * *.

In the following findings with respect to what the advertisements of respondents in question would mean, the hearing examiner has given consideration to the foregoing principles as well as the following ones: "(W)hatever statements are made, must be taken with and accepted in their ordinary sense." *DeForest's Training, Inc. v. F.T.C.* (C.C.A. 7, 1943), 134 F. 2d 819, 821. "Words mean what they are intended and understood to mean." *Bennett, etc. v. F.T.C.* (C.A.D.C., 1952), 200 F. 2d 362, 363. The Commission cannot interpolate language into advertising that is not there in order to construe it as misleading. *International Parts Corp. v. F.T.C.* (C.C.A. 7, 1943), 133 F. 2d 883, 888. "Advertisements must be considered in their entirety and as they would be read by those to whom they appeal." *Aronberg v. F.T.C.* (C.C.A. 7, 1942), 132 F. 2d 165, 167. See also *Ford Motor Co. v. F.T.C.* (C.C.A. 6, 1941), 120 F. 2d 175, 182, cert. denied 314 U.S. 668. "The important question to be resolved is the impression given by the advertisement as a whole * * * (A)dvertisements which create a false impression, although literally true, may be prohibited." *Rhodes Pharmacal Co. v. F.T.C.*, 208 F. 2d 382, 387, and authorities cited. If the advertising has a capacity and tendency to deceive there is no requirement that anyone be actually deceived, or that there was an intent to deceive.

In determining the facts in this proceeding upon the whole record as required by law, the hearing examiner has given full and impartial consideration to all the evidence and to the fair and reasonable inferences arising therefrom. He has carefully examined the pleadings and found those facts alleged in the complaint and admitted by the answer to be true. Thus, upon consideration of the whole record, including the factual matters already referred to, and, from his personal observation of the conduct and demeanor of the witnesses, the examiner makes the following:

FINDINGS OF FACT

Respondent, Federal Employees' Distributing Company, Inc., is a corporation existing and doing business under, and by virtue of, the laws of the State of California, with its principal offices at 2944 East 44th Street, Los Angeles, California, and its principal place of business or merchandise store located at 3928 West Slauson Avenue, Los Angeles. It also has four other such stores elsewhere in Southern California. It is a "non-profit" corporation (respondents' Exhibit 18) under Section 9200 of the Corporations Code of the State of California, which provides:

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A nonprofit corporation may be formed by three or more persons for any lawful purposes which do not contemplate the distribution of gains, profits, or dividends to the members thereof and for which individuals lawfully may associate themselves, such as religious, charitable, social, educational, or cemetery purposes, or for rendering services, subject to laws and regulations applicable to particular classes of nonprofit corporations or lines of activity. Carrying on business at a profit as an incident to the main purposes of the corporation and the distribution of assets to members on dissolution are not forbidden to nonprofit corporations, but no corporation formed or existing under this part shall distribute any gains, profits, or dividends to any of its members as such except upon dissolution or winding up.

Respondent David D. MacFarlane is president of the corporation; respondent A. Patrick Harrison is its vice-president; respondent Francis M. Bishop, its treasurer, and respondent Samuel W. Patterson, its secretary. These four constitute all the officers of the corporation and they are also members of the Board of Directors, which also is comprised of several other members of this non-profit corporation. All of the individual respondents reside in Southern California. It is undisputed that the Board of Directors, including the individual respondents herein, formulate, direct, and control the policies, acts, and practices of the corporate respondent, which trades under the name of FEDCO, Inc. It so trades by and through another California non-profit corporation "FEDCO, Inc." (see respondents' Exhibit 19), which was organized by respondents in 1954 for the purpose of effectuating, protecting, and preserving the trade name of FEDCO, which is the name under which the respondent corporation had built up its goodwill. It not only does its commercial business under that name but by that name alone it is known to or recognized by its membership at large or to those members of the outside public who are eligible to membership therein and to whom advertising relating to attaining such membership may be appealing. The corporation uses the name FEDCO on all its business forms, such as envelopes, letterheads, sales slips, and interoffice forms. It uses this name exclusively, in its signs both inside and outside of its several stores. It has used the full corporate name of Federal Employees' Distributing Company, Inc., only in official documents and where it has been advised by counsel that the law requires the use of such name since the long regular name of the corporation had no commercial value and was cumbersome. A large number of the exhibits in the case are current photographs of the exteriors and interiors of respondents' several stores where the name FEDCO appears on the large signs and other insignia and nowhere does the long regular corporate name appear. (See respondents' Exhibits 23 to 28, incl. and 37 to 51, incl.)

The history of the corporation is quite interesting and illustrates the phenomenal growth that is possible in a cooperative enterprise under the economic conditions which have prevailed generally the past ten years or so. In August 1949, a small group of federal employees in the Los Angeles area, realizing that there was then little prospect of an increase in pay to federal employees generally despite the rapidly increasing cost of living, organized the respondent corporation, whose principal purpose was to procure and distribute household appliances to federal employees at prices below those which prevailed in the Southern California area. They, therefore, incorporated under the provisions of Title I, Division II, Part I, Article II of the Corporation Code of the State of California as a non-profit corporation. The material section of the California Corporation Code, Section 9200, has hereinbefore been fully quoted. The charter of respondent corporation sets forth its purposes in detail (see Respondents' Exhibit 18). Its express purposes were set forth in Paragraph IV of its Articles of Incorporation and include two general basic purposes: (1) the fostering and cultivation of the social, educational and business relations of the members, the broadening of their interests in their occupations, the improvement of their standards of efficiency and production, a closer personal acquaintance, a friendly spirit of mutual cooperation, the gathering and disseminating of valuable information to its members including mutual assistance and vocational guidance, and the general welfare and prosperity of its members; and (2) the procurement of goods, materials, and services through cooperative effort and combined buying power of the members, thereby to effect savings for its members for their mutual benefit, and the purchasing, leasing, etc. of real and personal property, the carrying on of a general merchantile or merchandise business as well as the buying, selling, and dealing generally in all classes of goods, wares and merchandise and articles of trade, and the purchase, lease, etc., of necessary stockrooms, warehouses, and stores to effectuate such purposes.

At the commencement of this corporation some 200 federal employees each contributed a \$2 membership fee for a lifetime membership in respondent corporation. With this small capital, business naturally began on a very small scale. There was a small store and only one paid employee, the directors and other members helping in their spare time until the business got underway. Customer members ordered their merchandise from catalogues, and the respondent corporation ordered these specific items from manufacturers or dealers, and when the item had been produced the purchaser paid the item price plus 5 percent, which was an arbitrary figure to cover the cor-

poration's cost of doing business. As the membership increased, it became necessary to enlarge the company's quarters, to hire more assistants, and some of the officers found it necessary to give up their government employment and spend full time in connection with the business. While there have been some changes in the official personnel, the membership in attendance at the Annual Meetings, empowered by the charter and by-laws to vote in person or by proxy, have found the methods of operation so satisfactory that some of the officers and directors have continued throughout the approximate ten years of corporate existence. The membership continued to grow rapidly, and, since the profits of the corporation could not be distributed, they were eventually employed in expanding the business, which then moved to much larger headquarters, and finally led to the establishment of four large additional stores in the Southern California area.

In 1956 the pressures upon the corporation to enlarge the classes of persons eligible to membership were finally yielded to. At that time the corporation had approximately 200,000 members. Associate memberships were then provided for and "issued only to persons on the payroll of any of the several States or Territories of the United States of America or any employee of any political or municipal subdivision of such States or Territories, either in an active or a retired status" (R. Ex. 17, p. 1). Regular memberships were confined as before "to persons on the payroll of the Government of the United States of America, either on an active or a retired status, and to persons regularly receiving disability compensation or pensions through the United States Veterans Administration" (*Id.*). Honorary memberships were also granted at the same time in a limited number, but all voting power was vested exclusively in the holders of regular memberships (*Id.* p. 2). Any assets remaining on dissolution, however, were distributable pro rata to the then holders of regular and associate memberships (*Id.* p. 3). In 1958 there was a further expansion of the associate memberships "to employees of non-profit corporations organized and operating exclusively for educational, scientific or religious purposes" (R. Ex. 16, p. 1).

While the corporation's business is mainly retail sales made directly through its five stores in Southern California, it also makes occasional sales throughout certain States of the United States, including the former Territory of Alaska, and Guam. It does not, however, in any way purport to be or operate as a mail order company, its sales being for the pure accommodation of its members, and the evidence shows that these sales are only occasional and total but

about one percent of the business. Respondent corporation operates its said stores much as regular mercantile establishments do. Its officers are paid substantial salaries which are not out of line with those of comparable institutions and they devote their full time and attention to the management of such stores. The employees, such as salespeople, warehouse workers, etc., are union-organized and receive union wages under appropriate contracts. The respondent corporation pays regular federal corporate income taxes annually as well as state corporate income taxes to the State of California. The general manager is paid a straight salary plus a percentage based on the annual sales. In addition to its retail sales, respondent corporation receives as part of its income rent from concessionaires in its stores and income from advertising space purchased by manufacturers for their ads in The Fedco Reporter.

Respondent corporation extends credit in certain instances and makes credit loans on purchases of large items in collaboration with certain local California banks. It also has its own credit system for smaller purchases by the use of a so-called FED SCRIP which it handles within its own organization on special accounts. While delivery and installation services are furnished to member customers, such charges are not included in the listed and posted prices of merchandise as special arrangements and charges must be made for such services. Respondent corporation pursues its defaulting debtors in order to clear balances due it in substantially the same manner as any other retail mercantile store would do.

From a meagre 200 members at the time of organization in 1949, with a small one-room store, the rental for which was \$85 per month, and had but one paid employee, in a short decade, the company, as shown by the record, had developed into a large organization of over 360,000 members with five large retail stores, and from 325 to 500 paid employees who are dealt with by the corporation through union contracts. In January 1957 it had assets aggregating nearly \$4,000,000, capital arising from its \$2 membership fees of nearly \$600,000, and an earned surplus from its business operations of over \$1,600,000. Reference has already been made to the gross business of the corporation which aggregated \$30,000,000 in 1958. Growth in the early years was not rapid but was progressive and has rapidly expanded in the last six years as shown by numerous exhibits in evidence. To illustrate this, on November 21, 1953, there were 50,623 members; on April 22, 1955, 93,055; on April 23, 1956, 145,902; on November 26, 1956, 185,433; on April 15, 1957, 212,078; on February 10, 1958, 278,060; in April 1958, over 300,000; and at time of trial on March 2, 1959, approximately 360,000 (See Respondents' Exhibits 2-15,

20-22, 65, 69; R. 76 and 106). The number of Fedco Reporters mailed out monthly has naturally lagged somewhat behind the actual membership but the record discloses that up to June 1958, the total mail circulation of all such publications had been over 7½ million copies. A few copies are handed out in the stores but they are not mailed to non-members, the membership growth depending upon word-of-mouth, the members' privilege of bringing in two guests at a time to visit the stores, and the inclusion of an application form in the monthly magazine which members are occasionally urged to present to and have executed by their eligible friends.

This extraordinary growth of the membership of this particular corporation is probably a phenomenon best explained by two fundamental factors: (1) the rapidly increasing population and economic development of Southern California, and (2) the business policies of respondent corporation: (a) in keeping advised as to the level of retail prices in Southern California of the various commodities it handles; (b) in selling at anywhere between ten and fifty percent below the going retail rates for such commodities in that area; and (c) in not carrying any items for sale in its stores on which it cannot undersell its competition. Other facts particularly relevant to the specific charges of misrepresentation involved herein will be stated pertinently in connection therewith.

The complaint charges, paragraphs 4 and 5, that for the purpose of developing their business and encouraging the sale of products sold by them respondents have falsely represented and are now falsely representing to the general public and to its membership, both directly or by implication, that (a) said business is connected with, or sponsored by, the Federal Government; (b) that membership is limited to individuals employed by, or connected with, the Federal Government; (c) that only those persons who have paid a \$2 membership fee may purchase merchandise at respondents' stores; (d) that corporate respondent is a non-profit corporation and all profits are passed on to the purchasing members; and (e) that the retail price of merchandise is its cost to respondent corporation plus five percent. All of these allegations are specifically denied by respondents, paragraphs IV and V, of the answer. Each will now be considered in the order in which it is alleged.

As to the alleged claim of respondent corporation's connection with or sponsorship by the Federal Government, counsel supporting the complaint relies chiefly upon the use of the word "Federal" in the corporate title, Federal Employees' Distributing Company, Inc. Respondents contend that in all of their dealings with the public, except where reference to the exact corporate name is necessary, said cor-

poration has used the name and style of FEDCO, has had that name adopted officially as a trade name, has formed an operating corporation under that name, and has protected it in divers actions in the California courts. It further contends that in no event is the use of the word "Federal" illegal or deceitful. Counsel supporting the complaint, in addition to several general principles of Federal Trade Commission law, with which respondents do not disagree, relies chiefly on the following cases: *Federal Coaching Institute*, 49 FTC 1138 (1953); *The Capitol Service, Inc.*, 51 FTC 198 (1954); and *F.T.C. v. Army & Navy Trading Co.*, 21 FTC 541, 88 F. 2d 776 (C.A.D.C., 1937). Respondents correctly argue that these cases are not in point. Careful analysis shows that in each of them a private corporation organized for individual profit was using advertisements and literature definitely indicating a connection with the United States Government. *Federal Coaching Institute* and *The Capitol Service* cases, *supra*, each involved the sale of correspondence courses to prepare students for U.S. Civil Service positions, unmistakably indicating the seller's connection with the Federal Government itself, which alone can provide such Civil Service positions. In the latter case, it also appeared that sales agents made certain other false representations and that the advertising material picturized the dome of the U.S. Capitol under such conditions as to mislead prospective purchasers to believe that there was some connection between that respondent and the United States Government. Even in that case the use of the picture was not prohibited, but was permitted if accompanied by words stating clearly that respondent was a private correspondence school. In this latter connection, counsel supporting the complaint urges that the membership and the public dealing with respondent corporation are misled by a small picture of a domed building back of the column in *The Fedco Reporter* called "Washington Report," by the well-known Washington correspondent Jerry Kluttz, whose syndicated column on matters of special interest to federal employees appears in the *Washington Post* and other publications. The examiner has carefully considered Mr. Kluttz's column and the heading thereof and does not believe that the picture of the building there shown would mislead any person into believing that Jerry Kluttz was the Federal Government or that his report on proceedings in Washington affecting federal employees was a part of the official acts of the Government of the United States. This is also true as regards a large picture of the Capitol in Washington, which appeared only once on the outside cover of the July, 1958, issue of *The Fedco Reporter*. In the *Army & Navy Trading* case, *supra*, there were false representations that Army and Navy goods were for

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sale when a very small portion of the merchandise carried by the respondent were such goods. The use of the words "Army" and "Navy," of course, clearly implied official connection. Nor are other cases cited by counsel supporting the complaint relevant to the case at bar—*A.P.W. Paper Co. v. F.T.C.* (C.C.A. 2, 1945), 149 F. 2d 424, prohibiting the use of the term "Red Cross," and *Perloff v. F.T.C.* (C.C.A. 3, 1945), 150 F. 2d 757, prohibiting the use of the term "packing" where respondent was not a packer. It is also to be noted that in at least some of the foregoing cases consumer witnesses testified they were deceived by the advertising there in question.

Respondents' counsel has carefully analyzed all Commission cases involving the word "Federal," stating in their brief (p. 32): "During the period 1916 to 1958, the FTC instituted approximately 33 proceedings against respondents whose name began with the word 'Federal.' In 27 of these 33 proceedings, the word 'Federal' in respondents' name appears to have been ignored by the Commission." Counsel supporting the complaint does not challenge this statement. The remaining six cases are thereupon carefully analyzed and reveal that the word "Federal" standing alone is not *per se* deceptive, but must be used in connection with other words clearly connoting Governmental connection. In *Federal Civil Service Training Bureau*, 25 FTC 444 (1937), we have another Civil Service advertising case such as those above referred to. In *Federal Military Equipment Corp.*, 43 FTC 357 (1943), the advertising indicated that respondent was selling federal military equipment. In *Federal Organization, Inc.*, 29 FTC 504 (1939), respondents used a seal which stated their product was "a certified federal product approved by the Federal Research Laboratories * * *." In *Federal Institute of Meats & Marketing*, 24 FTC 199 (1936), a mail order correspondence course in butchering, respondent, located in Michigan, had its letterhead labelled "Central States Division Federal Institute—Meats—Marketing, Washington, D.C." with the name of its owner as the "Divisional Director" in the "Central States Office." In *Federal Bond & Mortgage Co.*, 8 FTC 194 (1924), it was held that the bonds offered were *per se* deceiving, respondent offering bonds referred to as "Federal bonds" throughout all its advertising. The sixth case is *Federal Coaching Institute*, *supra*, already referred to as a correspondence course providing Civil Service training. In most of these cases there was evidence that the consuming public was in fact deceived. In any event they are all clearly distinguishable from the use of the word "Federal" as respondents have incorporated it in their official corporate title here. There has been no flagrant attempt to use this name as a flamboyant "lead" to sell merchandise, and the record dis-

closes that the coined word "FEDCO" has been used almost exclusively in all of respondents' advertising matter as well as in all signs within and without all of their retail stores. The necessary, unemphasized small-type references in the monthly Fedco Reporter to the fact that it is published by the Federal Employees' Distributing Company, or in the application-for-membership forms do not appear to be deceptive. The word "Federal," as urged by respondents, is always modified by the word "Employees" wherever it does appear, and certainly the term "Federal Employees'" does not connote ownership by the Federal Government, as its employees are definitely individuals clearly distinguishable from the Government itself. The use of the full corporate name in the life-membership cards is required by California law, since such cards constitute securities under the California Corporations Code, and their issuance must be approved by the Corporation Commissioner. At any rate these membership cards are received by members after they have joined and not prior thereto; hence, it cannot even be found that they constitute a representation to procure members, let alone that they are misleading to the public in any way.

It is urged by counsel supporting the complaint that the term "Federal" should not be used "in any form or fashion directly or indirectly" by respondents as the use of this word is a fraud upon the public. He proposes that the use of the word "Federal" be prohibited. This corporate title has been used and employed by respondents for ten years; they have not misused it; this name was authorized by the California law, and approved and reapproved repeatedly by the proper California regulatory authorities. Of course this does not mean that the Federal Trade Commission is powerless to act if practices in commerce violate any law which it has the duty to enforce. See *Royal Oil Corporation v. F.T.C.* (C.A. 4, 1959), 262 F. 2d 741, 743, and cases cited. Excision of a corporate trade name is required only when no less drastic means can accomplish the protection of the public. See *Elliot Knitwear, Inc. v. F.T.C.* (C.A. 2, 1959), 266 F. 2d 787, 790-791, and cases cited. The word "Federal" has been, and is being, used by countless corporations and others throughout the country, just as the words "National," "Government," and "United States" are used. One needs only to look in the telephone directory of nearly any city of substantial size in the United States to see dozens of concerns using such words in their names. Does anyone for a moment believe that Government Employees Insurance Companies are agencies of the Federal Government or that U.S. Steel, U.S. Rubber, the National Broadcasting Company, Federal Storage Company, or National Bis-

cuit Company are Government corporations and not private enterprises?

All of the advertising matter used by respondent corporation has been carefully read and analyzed by the hearing examiner and he can find nothing therein which in his opinion tends to deceive or mislead the public with respect to this charge, and concludes with respect thereto that no eligible person has been, or can be, misled by the respondents' use of the name "Federal Employees' Distributing Company" into believing that this organization is connected with or sponsored by the Federal Government. Such name is only used by respondents where it is legally required, and it is not emphasized or placed in deceptive context anywhere. He therefore finds that respondents have not represented that the corporate respondent or its business is in any way connected with or sponsored by the United States Government.

The second charge is that respondents have falsely represented by their advertising matter that their membership is limited to individuals who are employed by, or connected with, the Federal Government. While counsel supporting the complaint concedes that as originally intended and first organized the respondent corporation was a service to a group of federal employees, he contends that now by reason of its growth and practices it is no longer such an organization, but has become a regular commercial "discount house" which, under the cloak of its original corporate charter, is misleading to the purchasing public and unfairly diverts trade from its competitors. The evidence pertaining to the expansion of the corporation's membership has heretofore been fully set forth. Respondents meet this issue in their answer by admitting that in prior years they did represent the corporate membership was limited to employees of the Federal Government, but deny each and every other allegation pertaining to said charge. The record discloses that each time the class of membership has been changed respondents have correctly advised all persons concerned of such change through their regular monthly publication, and that such changes have been duly made by appropriate amendments to the by-laws through legitimate action of the board of directors. Nothing in the corporate charter limits the corporate membership to present or former Federal employees, and, the by-laws having been appropriately amended to include new classes, the question then arises as to who can properly complain thereof, if anyone. Certainly the members who are already a part of the corporation cannot make complaint, and even if they had any valid complaint that the corporate officers had acted wrongfully in expanding the original membership, their remedy would appear to

be a judicial one in the courts of California, not a proceeding before the Federal Trade Commission. Counsel supporting the complaint does not make clear as to just how the outside public, who theretofore had not been eligible to membership, can properly complain or why the Federal Trade Commission should complain on their behalf. There certainly have been no false representations with respect to the classes of persons eligible to membership. To the contrary, they have been openly and correctly stated at all times, as hereinafter specifically found.

Prior to February 26, 1955, of course, there had been only one class of members, present or former U.S. Government employees—as the membership application forms then in force made manifest. On said date the board of directors received a report of its legislative committee proposing an amendment of Article I of the by-laws creating associate memberships for the first time. Honorary members are not important herein, since they paid nothing and were limited to an authorized maximum of 12 per year (R. Ex. 15). Actually, a half dozen such memberships have been granted “during the lifetime of the corporation” (R. 64-65). Subsequently the by-laws were amended in accordance with Article VII thereof, and the several classes of memberships were duly set forth in Article I as appears in respondents’ Exhibit 17 under date of November 1, 1956. The associate memberships thereby provided for could “be issued only to persons on the payroll of any of the several states or territories of the United States of America, or of any political or municipal subdivision of any such states or territories, either in an active or retired status” (R. Ex. 17, p. 1, Art. I, §1(b)). Thereafter the classes of persons who might obtain associate memberships were further expanded to include “members of non-profit corporations organized and operated exclusively for educational, scientific, or religious purposes” (See R. Ex. 16, by-laws, as of March 22, 1958, Art. I, §1(b)).

The Fedco Reporter had properly published eligibility for corporate membership prior to any of these by-law amendments by stating that the applicant was required to be “on the payroll of the Government of the United States, or on an active or retired status.” See Fedco Reporter, February 1954, p. 10, R. Ex. 60; *idem*, July, 1954, p. 9, R. Ex. 6; *idem*, August, 1954, p. 8, R. Ex. 62; and *idem*, February, 1955, p. 10, R. Ex. 63. It is noted that in said February, 1955 (R. Ex. 63) publication a warning appeared at page 7, “Please do not sign a membership application for any person who you are not personally sure is an employee of the Federal Government.” As already stated, in February, 1955, consideration was given to enlargement of the membership, which thereafter became effective. All

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concerned were fully notified of this change when it had been effected. See R. Ex. 64, p. 1, Col. 1, June, 1955 Fedco Reporter. Also, on page 12 of the July, 1955, issue of the publication, R. Ex. 65, the application form had been expanded to include the associate membership eligibility of state and local subdivision employees. This was true also in the next issue of the Fedco Reporter, p. 12, R. Ex. 66. After the later expansion of the Associated membership in March, 1958, to include members of certain types of non-profit corporations, the Fedco Reporter issues for March and subsequent months in 1958 (in evidence as Respondents' Exhibits 59 and 68 to 71, inclusive), each sets forth in a heavy-type column near the membership application form a clear, specific statement as to just who is eligible for FEDCO membership, and the application forms have been amended to include all such new classes of memberships.

In order to sell its memberships, the corporation was required to advise the California Corporation Commissioner just what the eligibility qualifications for corporate membership were before a permit would be granted for the issuance and sale of such membership certificates. Respondents' Exhibit 2 recites the original regulations regarding membership qualifications. Their Exhibit 3, dated April 22, 1955, shows the addition of associate memberships of state and municipal subdivision employees, while their Exhibit 14, dated February 10, 1958, sets forth the additional group of non-profit corporation employees who are eligible for membership.

The record abundantly shows that respondents, desiring that the corporation might grow, frequently gave precise information as to the qualifications for membership. This information was always factually correct at the time it was set forth in respondents' publications. There is, therefore, a complete failure of proof of the second charge, and it is found that respondents have not made any false, misleading, or deceptive representations, directly or indirectly, or deceptive representations, directly or indirectly, concerning the qualifications for membership in respondent corporation as charged in the complaint.

The third charge is that respondents have falsely represented that only those persons who have become members after paying a \$2 membership fee are permitted to purchase merchandise at corporate respondent's stores. It is true that the spouses of members may so purchase but if any unmarried member of respondent corporation might have such a specious objection, marriage would certainly cure any such inequality that might exist among the membership. As heretofore shown, other groups have been brought in to the corporation in recent years by virtue of the amendment of the by-laws. In

1956 the prior policy of not permitting guests to actually purchase merchandise in respondents' stores was changed and that subsequent thereto each member has been permitted to bring two guests who are permitted to buy on their own account. While members of families other than spouses have no absolute privilege of buying, they might enter the stores as guests. It is contended that this is an unfair practice in that the public has been misled into believing that they were gaining an exclusive privilege by paying a \$2 fee for membership. It does not appear that there has been any abuse of the guest privilege by any member or that such privilege has been denied to any member, and the argument of counsel supporting the complaint to the effect that this will bring in to respondents' stores the entire population of the area as customers, which practice would be unfair to the membership, seems far-fetched and without practical foundation. There is no evidence to indicate that if guests are permitted to purchase merchandise in the store members cannot get in or that there will be a shortage of merchandise for members desiring to buy the same.

In his brief, counsel supporting the complaint joins his argument upon this third charge with that relating to the second, and premises his contentions on both charges on the ephemeral conjecture that people pay a \$2 membership fee to join respondent corporation because of a "psychology of exclusiveness" or "snob appeal" which arises from respondents' advertising. This is a sort of argumentative shadow-boxing which is neither reasonable, practical, nor convincing. The examiner finds from this record that the sole reason eligible people ever joined this organization in such large numbers was to be enabled to purchase merchandise in respondents' stores at from ten to fifty percent cheaper than they could buy it elsewhere in the Southern California area. The corporation's extensive growth is in itself strong evidence that by and large they have been greatly satisfied and have spread the good news to their neighbors and friends. Respondent corporation never has been a social organization but only one which the Commission does not question actually provided high-class products at very low prices. Respondents' advertising shows that the brands of household equipment and other merchandise in many lines sold in the several FEDCO stores were leaders, such as, for example, Zenith, Philco, General Electric, and RCA-Victor television sets, and Admiral, Westinghouse and Hotpoint refrigerators. There is not a scintilla of evidence from which any fair and reasonable inference can arise either that any member ever joined the corporation except for the remarkable price advantages he expected to receive, or that merchandise and prices were not up to the advertisements thereof.

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Counsel supporting the complaint contends that this case is analogous to *Parke-Austin & Lipscomb v. F.T.C.* (C.C.A. 2, 1944), 142 F. 2d 437, cert. denied 323 U.S. 753, wherein the respondent, a private profit corporation which was a book publisher, made false and misleading statements in its literature and other aids supplied to its salesmen by which the public were falsely advised that the respondent was a representative of the Smithsonian Institution which was the real sponsor of the books being sold and the solicited person was one of a specially selected small and exclusive group. There is utterly no valid analogy between that case and the one at bar. Other differences are that sales in that case were made by door to door salesmen using respondents' false preliminary advertising as a basis for their sales pitches. In the case at bar under substantial security measures, only members, their spouses, and friends come into respondents' stores, buy what they actually see and want without any pressures whatsoever, as and when they choose, and they do so without any preliminary misrepresentations.

It is, therefore, found that respondents have not in any way deceived or misled their prospective members among the public or their current members at any time into believing that only those who held \$2 life memberships could enter and purchase merchandise in respondents' stores. The third charge of the complaint, therefore, is not sustained by the evidence.

The fourth charge is that in their advertising respondents have falsely represented to the public that the corporation is a non-profit corporation. Respondents have not challenged the Commission's jurisdiction upon the ground they were not a profit corporation with the definition of "corporation" in §4 of the Federal Trade Commission Act (R. 396). Respondent corporation is in fact a non-profit corporation duly organized and existing under the non-profit corporation statute of California, already quoted herein. There can be no question whatsoever as to the non-profit character of respondent corporation under its charter. The said non-profit corporation law of California is rather unusual. The language of the statute provides that such a corporation "may be formed by three or more persons for any lawful purposes which do not contemplate the distribution of gains, profits, or dividends to the members thereof and for which individuals lawfully may associate themselves." Certainly the business of respondents is a legitimate one. It has not been pointed out that it is unauthorized under California law or that the general nature of its business is in any way immoral or illegal. The sole charge is that the advertising practices are false, misleading, and deceptive under the Federal Trade Commission Act. A cursory ex-

amination of the many judicial decisions of the California Supreme Court and Courts of Appeals, under this non-profit corporation law, as collated in Volume 25, West's, Annotated California Codes, §§9200 et seq., reveals that many types of business organizations have been recognized by the California judiciary as being non-profit in character. In his argument, however, counsel supporting the complaint erroneously equates any corporations organized under this statute with eleemosynary corporations. It is true the statute says by way of illustration immediately after its language just above quoted: "such as religious, charitable, social, educational, or cemetery purposes." Certainly such corporations are authorized by and do exist under this statute. But immediately after the foregoing quoted language the following language also appears: "or for the rendering of services, subject to laws and regulations applicable to particular classes of non-profit corporations or lines of activity." This language clearly indicates that a non-profit corporation may be organized for the purpose of rendering any lawful services and that is exactly what the basic purpose of respondent corporation appears to be. Not every corporation that is non-profit is a charitable corporation. Whether or not a corporation is one for pecuniary profit or one of non-profit character depends, of course, upon the particular statute under which it is organized, but as a general proposition of law "non-profit corporations are not confined to those which are eleemosynary or charitable, but include business or auxiliary corporations not for profit, as well"—Volume I Fletcher's Cyclopedia of Corporations, page 238, §68 citing numerous cases. The California statute under consideration here has been given a like practical construction for many years by the authorities charged with its administration. And, specifically, respondent corporation here has not only been chartered as a non-profit corporation under said law (respondents' Exhibit 18) but has repeatedly appeared during a number of years before the Department of Investment, Division of Corporations, of the State of California, as a non-profit corporation under this statute and has been specifically authorized as such to issue membership certificates each time it has altered its membership qualifications or otherwise needed the issuance of additional certificates because of its increasing membership. (See respondents' Exhibits 2-14, inclusive.)

Another unusual feature of the said California statute is that it definitely recognizes the fundamental truth that no corporation, even one not organized for profit, unless richly endowed, can long survive and carry out its purposes unless it takes in more money than it expends. The statute expressly provides that no corporation formed or existing thereunder "shall distribute any gains, profits, or

dividends to any of its members as such except upon dissolution or winding up." Here it is contended, however, by counsel supporting the complaint that the advertisements in the San Diego newspapers at the time of the opening of respondents' store there in October, 1957, tend to mislead the public into believing that respondent corporation is a stock corporation declaring profits because of an expression in its large ads contained in such newspapers. The particular statement attacked is: "FEDCO is completely owned by its members. More than 240,000 lifetime owner-members are now collecting their dividends in the form of savings on all the purchases they make" (See Commission's Exhibits 8, 9, and 10). It is argued that the word "dividends" clearly indicates to the public a profit corporation, presumably issuing shares of stock on which dividends are declared. This does violence to the actual language of the challenged advertisement which clearly limits the meaning of the word "dividends" to be "in the form of savings on all the purchases they make." At any rate there is no evidence as to the size and spread of the San Diego newspapers' respective circulations and no official notice can be taken that any substantial number of such publications ever crossed the boundaries of the State of California. Hence these publications in any view could not constitute a misrepresentation in interstate commerce. They did not advertise any foods, drugs, cosmetics or devices and would not establish a §12 case even if mailed in large numbers within the State of California.

Of course, it is the general rule that in determining a corporation's character for tax or other purposes the charter is not necessarily controlling. It might be a charitable or non-profit one but still be held liable for taxes, for torts or otherwise (see Annotation 119 A.L.R. 1012, 1022-1027). Cooperative corporations have become quite numerous in recent years where there are no "profits" as such but where there is a distribution or accumulation of savings made through the cooperative operations (see Vol. I Fletcher's Cyclopaedia of Corporations, p. 398, §109). Many corporations of this character which are non-stock corporations conduct certain business operations and are still held not to be a corporation for profit (see Annotation 16 A.L.R. 2d 1345, 1349-1350).

There is no evidence that respondents have in any way violated the California statute by distributing profits to their members except in the form of such savings as they may effect in buying merchandise at respondents' stores. And respondents contend that with the expanded membership and increased buying power these savings naturally become greater and more assured.

Counsel supporting the complaint contends that the purchasing

public would not know that respondents are not permitted to distribute any gains under the California law but believe that a non-profit corporation does not keep its profits and therefore should sell at absolute cost. The examiner is unable to follow this reasoning as such counsel has also argued that a non-profit corporation is of necessity a charitable organization. If so, how can it have any profits? And why would the people believe that it would distribute profits? The simple truth is that no one believed, because of the non-profit character of respondent corporation, that in joining it they were joining a charitable organization, or that the \$2 lifetime membership fee would entitle them to go into respondents' stores forever and receive free merchandise. At least the orthodox view of charitable organizations is that they do not receive any moneys for the services they render or the clothes, food, and other articles they distribute to the poor and needy. Of course, even under California law when in the operation of a business charitable institutions make earnings over and above actual expenses of operation they are taxed like any profit corporation (see, for example, *Sutter Hospital v. City of Sacramento* (1952), 39 Cal. 2d 33, 244 P. 2d 390, where the hospital was held not entitled to a tax exemption since it is operated for the purposes of producing a surplus to retire bonded indebtedness and expand existing facilities). It is urged by respondents that the expertise of the Commission does not permit it to speculate upon what the public believes a non-profit corporation can do under any statute, the California statute in particular. It is not necessary for the examiner to resolve such a question however, since the respondents did not use the term "non-profit corporation" in direct connection with the advertisement of their goods but only where the law required, such as in the certificates of membership or in the statement in the magazine as to who the actual publisher was. Since it was merely stating the truth when it said it was a non-profit corporation and there was no effort to use such language to mislead the public, the examiner does not find that such legal use of the term in such limited ways is false, misleading, and deceptive. As already stated, in substance, people take out memberships in respondent corporation in order to procure high class merchandise at low prices. Of course, as they advertised in opening the San Diego store the membership received their dividends, not in the form of a check but "in the form of savings on all purchases they make." Furthermore, the facilities and services are brought closer to the membership when respondents open new stores from time to time which are effectuated by the use of any surpluses left in the corporate treasury above the cost of doing business. This in turn passes on more savings to more mem-

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bers, and the examiner can see utterly nothing deceitful or unlawful in such business activities. It is urged, in essence, by counsel supporting the complaint that the management can not only earn a comfortable living but can pay themselves bonuses and otherwise unjustly enrich themselves. The ten-year record of this corporation does not support any such unjust inference respecting the individual respondents, but in any event the Federal Trade Commission has no jurisdiction to take over and regulate the internal affairs of respondent corporation, its authority being strictly limited to finding they have engaged in unfair practices which are deceitful of the public which is the basis of the present proceeding.

The cases relied upon by counsel supporting the complaint on this fourth charge are not in point. In *National Secretaries Assn., et al.* (1945), 40 FTC 352, a non-profit corporation was organized and incorporated as not for profit but was actually operated by its officers as a private business to promote the sale and distribution of their own books for profit. In the matter of *Albert Lane t/a Consumers Bureau of Standards* (1941), 32 FTC 1330, (C.C.A. 9, 1942), 130 F. 2d 48, it was held that respondent's claim that he operated as a non-profit trust gave the Commission no jurisdiction over him as invalid as the business actually was operated as purely one for private profit although advertised as a non-profit consumer research and educational organization; and in *Educators Assn. v. F.T.C.* (C.C.A. 2, 1939), 108 F. 2d 470, rehearing denied 118 F. 2d 562, respondents represented to purchasers that their books were published by non-profit concerns whereas in fact such books were sold for the private profit of the president of respondent corporation.

It is also urged that the recent decision in *Gov-Mart, et al.*, Docket No. 7049, is authoritative in the case at bar. The evidence there insofar as it proceeded in contest reveals a very different state of facts from those presented here and is therefore not in point. But in any event that case resulted in a consent order under agreement of parties and is not a precedent in other cases for any purpose. For the same reason counsel supporting the complaint cannot rely upon the consent order decisions in *Universal Training Service* (1955), 52 FTC 298, and *Oklahoma College of Audiometry, et al.* (1955), 52 FTC 558.

It is, therefore, found that the respondents have not falsely represented in any way that the corporate respondent is a non-profit corporation and that all profits earned are passed on to its purchasing members. Under its charter, of course, the said corporation, in event of its dissolution, would distribute its assets equitably among the then surviving voting and associate members. The fourth charge of the complaint should be dismissed.

The fifth charge of the complaint is that respondents have falsely represented that the retail price of merchandise sold in the corporation's stores is the cost of such goods to said corporate respondent plus five percent. This charge has been apparently premised on statements made in the Fedco Reporters for September and October, 1957 (Commission's Exhibits 1 and 2). In connection with the indicated price of merchandise advertised on page 2 of each of said publications appears the following: "Note: To all prices add 5% and 4% sales tax." This is preceded by an asterisk and in the listed merchandise the cost follows the price thereof. Elsewhere in each of said publications there also appear similar asterisks with the expression at the bottom of the page following another asterisk: "Add 5% and sales tax." The burden of the argument of counsel supporting the complaint is that from reading such expressions in the advertisements those who were induced to purchase merchandise in respondents' stores believed they were paying its actual cost to respondents plus five percent and have not been informed either that there would be additional charges for delivery and installation of products bought or that the corporation was buying such merchandise in quantity for less than the unit price. It is urged that this belief was further engendered by references in respondents' monthly publication to its non-profit character, as hereinbefore discussed.

When the corporation started its business in a very small way, it could not afford to buy merchandise for display or to rent space in which to display it. It was at that time really nothing more than a catalogue house and the members of that small organization came, examined catalogues, and selected and ordered their choice of hard goods items, such as refrigerators and television sets. Then someone from the store would go to the supplier in another part of the city, buy such article at the unit wholesale price, and bring it back to the store where the purchaser, after being notified it was ready, came and paid for it and transported it away. The practice grew up, therefore, of taking such catalogue unit price of any hard goods items, adding five percent thereto to cover the estimated cost of the store's operations, and giving the customer of an item two figures, one the actual unit cost and the other five percent thereof, the total of which was the price to him. There is no evidence in the record that the members were ever advised as to what the first figure meant or just why the combination of two figures was used. Their lack of capital and store space constituted the necessary and natural historic reason for setting prices in this manner in the early days of the business. As operations increased and business grew, however, the purchasing power became greater and display and storage space was

available so that by gradual stages the corporation was enabled to purchase and carry in its own stock substantial amounts of these hard goods products to display and sell right in the store. Respondents were then financially able to buy from the wholesaler or supplier at quantity discounts. Price tags on merchandise throughout the store, however, continued to carry a stated figure with an added five percent indicated thereon. It was stipulated that merchandise is sold by corporate respondent to its members at a retail price substantially in excess of five percent of the invoice cost of such merchandise to corporate respondent, and there is no claim by respondents that this markup is merely *de minimis*. The issue is not what the retail prices actually were but whether they were misadvertised by respondents.

During her investigation, on September 23, 1957, the Commission's attorney-examiner, Marita Kellum, entered the respondent's Lakewood branch store in Los Angeles with a friend her guest, and purchased some items of merchandise. It appears that both on the merchandise tags and on the adding machine slips she received in connection with her purchases that 5 percent and the sales tax were added to the base figure, which constituted the total cost of the items to her. (See Commission's Exhibits 11-A, B, C and R, 132-134, and 197-198.) Whether Miss Kellum ever advised respondent officers or others in the employ of the corporation about such purchases does not appear in the record. It is inferred that she did not do so, since it was not only unnecessary but contrary to the general practice of the Commission for its investigators to discuss the progress or findings of their investigation with the person under such investigation. It is therefore not inferred or found that cessation of these practices occurred because of the Commission's investigation.

At any rate, on November 23, 1957, by action of the board of directors, this practice of adding five percent to a stated figure as a pricing practice and advertising pertaining thereto was discontinued, effective as of January 2, 1958 (respondents' Exhibit 22, R. 255). The evidence shows there were three fundamental reasons for this action on the part of the board of directors. First, a recessionary period existing in late 1957 had created a competitive situation of much lower prices, particularly on hard goods, in the Los Angeles area, and the formula was no longer workable, as respondent had to reset prices based on the actual conditions. Unless it underpriced its competition it could not effect savings to its members, the prime cause of its very existence. Respondent's members are close shoppers and fully aware of going prices in their trading areas. Second, this pricing formula had long since ceased

to be practicable, since it had been established for the hard goods which were the only commodities sold in the early days of the company. They had expanded their operations to include soft goods, to which such fixed sales formula was inapplicable. Third, as the corporation grew, the clerical and bookkeeping expense of checking items, determining the five percent figure and adding it to the single unit price became burdensome and expensive. The last two reasons are continuing and permanent ones. Respondents have now taken over various concessions to which the former pricing practice could not apply, and have found greater efficiency and economy in selling on a "one-figure price" basis. It is extremely unlikely that there will be a resumption of such former two-figure pricing practice on their part. It no longer has any utility in the company's operations, and is wasteful and expensive to it in actual operation. The board of directors have also given every possible assurance that under no circumstances will they revert to such a practice, even offering to enter into a stipulation satisfactory to the Federal Trade Commission regarding such practice. The examiner, however, rejected such a proffer on the ground that it was an administrative matter over which he had no jurisdiction in a quasi-judicial matter (although from his observation of the witnesses he has utterly no doubt of the good faith of the offer). Such a pricing practice had been discontinued nearly a year before the instant proceeding was instituted. The facts clearly indicate that there is no reasonable probability that such a practice will be resumed. The evidence, therefore, comes within the criteria clearly recognized by the Commission for dismissal of charges on the ground of discontinuance in its recent opinions in *Ward Baking Co.*, Docket No. 6833 (June 23, 1958) and *The Firestone Tire & Rubber Company*, Docket No. 7020 (January 9, 1959) and cases cited in each of said decisions.

Even if the representations with regard to pricing were false, dismissal of the fifth charge on the ground of abandonment of such practices would, therefore, seem to be warranted in the exercise of a sound discretion. The examiner dismisses this particular charge, however, for a more basic reason. There is no proof that the respondents' advertising has ever misled or deceived their customer members into believing that this former pricing practice was the actual cost of merchandise to the corporate respondent plus five percent. It cannot be inferred reasonably that the addition of these two figures would lead the customers to believe that the five percent was only a handling cost while the basic figure was the actual

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cost to the corporation. The examiner disagrees with the contention of respondents that the drawing of inferences by the use of "expertise" can only occur where there is an intent to mislead, a patently false representation, or a previous line of decision condemning such pricing practice. The examiner merely finds that upon the evidence he cannot determine with any degree of certainty that the public believed what counsel supporting the complaint contends for. There is not a scintilla of evidence that anyone was concerned in the least with the two-figure price but only whether the total price to the purchaser was less than such purchaser could buy the product elsewhere. The positive evidence in the case given by respondents' officials negates any extreme inference that might possibly be drawn respecting this matter. Both treasurer Bishop and president MacFarlane testified positively that the corporation had never represented directly or indirectly, by any devices or advertising, that it sold merchandise at cost or at five percent above cost, and there was no cross-examination to break down these positive statements. To the contrary, the evidence shows that the cost of doing business had increased very substantially during recent years and that the corporate policy of selling to its customers at lower cost than they could purchase elsewhere has always kept down the actual cost of merchandise sold. The evidence contradicts any inference that respondents were interested in deceiving the public as to their actual price savings at respondents' stores over prices charged by competitors.

It is, therefore, found that the fifth charge is not sustained by the evidence and that respondents have never misrepresented in any way that the retail prices of merchandise sold by them is the cost of such merchandise plus five percent.

FACTUAL CONCLUSIONS

While the record is comparatively short, both counsel, by extensive and eloquent written and oral arguments and numerous proposals, have presented so many matters that to pass specifically upon each in this decision would unduly extend it. Only the basic contentions are sought to be determined herein. In concluding that counsel supporting the complaint has failed to sustain each of the five charges in question, the examiner has endeavored to apply the rule of reason to the evidence relevant thereto, viewed from the standpoint of those members of the public who were or are eligible prospective members of the respondent non-profit corporation.

While some Government employees and those of eleemosynary institutions certainly do not possess the superior intelligence of those in the highest offices and places, the examiner has preferred not to consider such persons as in an extremely low grade of intelligence, as appears to be urged by counsel supporting the complaint, but rather to consider them as the "unthinking, the ignorant, the credulous." An advertisement must be considered, it is true, in its entire context, i.e., "from its general fabric, not its single threads," as stated in *Ford Motor Co. v. F.T.C.* (C.C.A. 6, 1941) 120 F. 2d 175, 182, as counsel supporting the complaint has urged. But neither must it be given a technical, forced, or unnatural construction in order to sustain any charge. In the case at bar none of the challenged practices of respondent, either past or current, are false *per se*. To infer that any of them may have the capacity and tendency to mislead or deceive, such inferences must be based upon the evidence in the record fairly considered. "The 'expertise' of a commission usefully serves in evaluating the evidence, but that expertise cannot supply evidence" (*Capital Transit Co.* (C.A.D.C., 1953), 213 F. 2d 176, 185-187). The examiner, after careful deliberation under the foregoing principles and others quoted or referred to elsewhere herein, has not found that any of the prospective members of the respondent corporation have been in the past or could be in the future deluded in any way by the advertising statements alleged in the complaint to be false, misleading, and deceitful.

Furthermore, a fair consideration of the whole record reveals no facts establishing the existence of any real, substantial, and specific public interest in this proceeding. There is no evidence that respondents have charged those who bought merchandise improper or exorbitant prices, or sold them inferior goods, or otherwise deceived them by any advertisement or other alleged misrepresentation, and it does not appear that any person has ever made complaint of having suffered loss by reason of having been misled by the alleged unfair practices of respondents. The record affirmatively shows that the Commission's investigator devoted considerable time to the examination of respondent corporation's membership rolls; that she actually called upon and interviewed some ten members; that she took verbatim notes in shorthand of what they said to her; and that she then officially reported such matters to her superiors. During her testimony, upon objection, the examiner refused to direct her to produce her confidential notes. But the record shows that at the time she made her investigation in the fall of 1957 there were some 270,000 members of respondent corporation

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and that some 18 months later, at the time of hearing, such membership had increased to about 360,000, most of which vast membership lived within the Los Angeles area; thus many thousands of member customers were not far from the place where the hearing was held. But not one of them was called to testify. As aptly held in *S. Buchsbaum v. F.T.C.* (C.C.A. 7, 1947), 160 F. 2d 121, 123-124:

* * * We find in this record no evidence of any injury to any dissatisfied customer, indeed, there are no dissatisfied customers so far as this record discloses. It is intimated that the injury will occur to those who have been "long accustomed to the worth and use of glass." If this class of customers would consult their lexicons and inform the merchants as to the kind of glass they desire they will never be misled. Certainly they can not be misled or injured by petitioner's advertisements.

The Commission contends that actual deception of purchasers need not be shown in its proceedings, and that representations which have a "capacity" to deceive may be proscribed. This is quite true * * *. However, even though there be no proof of actual deception required, there must be a showing that the acts and practices sought to be proscribed are detrimental to the public interest in order to satisfy the statutory requirement that the proceeding be in the public interest (15 U.S.C.A. sec. 45(b)). Here the Commission made no finding that the deception, if any, had ever resulted in or had any tendency to result in detriment to the purchasing public. We find nothing in the findings to support the conclusion that the acts and practices are "all to the prejudice and injury of the public."

Counsel supporting the complaint has requested an order which, among other things, would prohibit respondent corporation from using the name "Federal Employees' Distributing Company" or any other similar name or contraction of any such name, and prohibiting any representation that respondents are "engaged in a non-profit enterprise." The most probable effect of any such an order would be to put respondents completely out of business for no demonstrable legal reason. The least that such a capricious order would do would require respondents to disrupt their entire organization and membership by reincorporating under a different statute and an entirely different name with great loss of business, good will, cash, and other assets. The examiner is loathe to exercise any authority for purely destructive purposes when the record discloses that respondents have created a vigorous competition in the Southern California area in the merchandise they deal in and have sold high class merchandise at extremely low prices. The whole purpose and trend of Federal legislation for the past seventy years has been to prevent monopoly and reduce the cost of commodities and services to the American public. To issue the drastic order

requested would violate these basic tenets of antimonopoly law and could have the probable effect of increasing prices to the public in Southern California. Certainly this Commission has no authority to change the statutory law of California. If respondent non-profit corporation is violating its charter, the only legal action available is *quo warranto* brought by the State of California itself (see *Vesper v. Forest Lawn Cemetery Assn.*, 20 Cal. A. 2d 157, 169, 67 P. 2d 368, 374, and cases cited). While it is insisted by counsel supporting the complaint that respondents' enterprise has become nothing more or less than an ordinary discount house, they vigorously deny this. In the examiner's opinion, it is immaterial what respondents' business may properly be called. It is in essence a buying service. Perhaps such a buying service is an unorthodox manner of doing business, at least when that business grows large enough to form an effective competition to others dealing in the same commodities in the same area. But unless the practices such an enterprise engages in are unfair in commerce, the Commission has no authority to proceed further. It is stipulated in the record that respondent corporation has competition, but only in Southern California. It is, of course, unnecessary to prove the existence of competition in commerce if unfair acts and practices in commerce are established (see *Progress Tailoring Co. v. F.T.C.*, *supra*, at page 105). But the Federal Trade Commission Act cannot be expanded by the examiner under quasi-judicial fiat merely in order to prohibit a California non-profit corporation from competing with others in ways that he or others might possibly believe to be unusual or distasteful. The expertise of an administrative agency does not empower it to rewrite the laws it is charged with enforcing, which is a function of Congress itself (see *Atalanta Trading Corporation v. F.T.C.* (C.A. 2, 1958). 258 F. 2d 365, 374).

Upon the findings of fact hereinbefore made, the examiner makes the following:

CONCLUSIONS OF LAW

1. The Federal Trade Commission has jurisdiction over the subject matter of this proceeding.
2. None of the respondents have committed any unfair and deceptive acts or practices, or used unfair methods of competition in commerce, within the intent and meaning of the Federal Trade Commission Act.
3. There is no clear, specific and substantial public interest in this proceeding.

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From the foregoing findings of fact, conclusions of law, and the evidence, the following order is hereby entered:

It is ordered, That the complaint be, and the same hereby is, dismissed in its entirety as to each and all of the respondents.

DECISION OF THE COMMISSION

The Commission having considered the hearing examiner's initial decision, filed on September 24, 1959, wherein the complaint in this proceeding was dismissed, and having determined that said initial decision is correct in all respects: