

Complaint

65 F.T.C.

IN THE MATTER OF

PUROLATOR PRODUCTS, INC.

ORDER, OPINIONS, ETC., IN REGARD TO THE ALLEGED VIOLATION OF SEC. 2 (a)
OF THE CLAYTON ACT

Docket 7850. Complaint, Mar. 29, 1960—Decision, Apr. 3, 1964

Order requiring a manufacturer of air, oil and fuel filters for trucks and automobiles, with nationwide distribution and net sales in 1957 in excess of \$37,000,000, to cease discriminating in price in violation of Sec. 2(a) of the Clayton Act by such practices as giving favored warehouse distributors "redistribution" discounts not granted to competing warehouse distributors and jobbers, on sales of its automotive replacement filters.

COMPLAINT

The Federal Trade Commission, having reason to believe that the party respondent named in the caption hereof has violated and is now violating the provisions of subsection (a) of Section 2 of the Clayton Act, as amended by the Robinson-Patman Act, approved June 19, 1936 (U.S.C. Title 15, Sec. 13), hereby issues its complaint, stating its charges with respect thereto as follows:

PARAGRAPH 1. Respondent Purolator Products, Inc., is a corporation organized and existing under the laws of the State of Delaware, with its principal office and place of business located at 970 New Brunswick Avenue, Rahway, New Jersey.

PAR. 2. Respondent is now, and for many years past has been, engaged in the manufacture, sale and distribution of a great variety of filters for use in the filtration of fuel, air, water and other liquids and gases. Applications for respondent's filters range from the air and fuel filters found on motor vehicles, through filters for hydraulic and cooling fluids, to industrial filters for use in the production and refinement of petroleum, chemicals and nuclear materials.

Respondent's total net sales for the year 1957 were in excess of \$37,000,000.

PAR. 3. Respondent manufactures filters in Rahway, New Jersey, and in other cities in the United States and ships them to its various customers located throughout the United States.

Respondent's customers have been divided, by it, into two classifications. The first, designated as the Equipment Sales Division, is composed of customers who incorporate respondent's filters in their own products or equipment and include such customers as automobile, truck and aircraft manufacturers, and chemical and petroleum producers.

The second, designated as the After Market Division, is composed primarily of customers who resell respondent's automotive filters (hereinafter referred to as "automotive replacement filters") as replacements for worn components on automobiles, trucks and other motor vehicles and include such customers as automotive parts distributors, truck fleets and oil companies marketing replacement parts under their own trade name.

In the sale and distribution of automotive replacement filters bearing the Purolator trade name to the replacement market, respondent ships said filters to a number of its selected, large volume, direct franchise distributors, classified by respondent as "warehouse distributors", located throughout the United States. Respondent also has a large number of associate distributors (hereinafter called "jobbers") who purchase said products from the direct franchise distributors. Respondent exercises such a degree of control over sales by direct franchised warehouse distributors to jobbers as to render such sales in all essential respects sales by respondent to such jobbers.

There is and has been at all times mentioned herein a continuous current of trade and commerce in respondent's automotive replacement filters across State lines, between their respective points of origin and respondent's customers. Said products are sold and distributed for use, consumption and resale within the various States of the United States and the District of Columbia.

PAR. 4. In the course and conduct of its business, respondent is now, and during the times mentioned herein has been, in substantial competition with other corporations, partnerships, individuals and firms engaged in the manufacture, sale and distribution of various types of filters.

Respondent's warehouse distributors are competitively engaged with each other in the sale of respondent's automotive replacement filters to jobbers and some users, and with each other and with jobbers in the sale of said filters to retailers (hereinafter called "dealers") such as service stations, garages and automobile dealers and to some users such as truck fleets, in their respective trade areas.

PAR. 5. Respondent, in the course and conduct of its business as above described, has been for many years last past, and presently is, discriminating in price between different purchasers of automotive replacement filters, by selling said products of like grade and quality to some of its purchasers at substantially higher prices than to other of its purchasers.

PAR. 6. Respondent has been, and now is, discriminating in price in the sale of automotive replacement filters of like grade and quality

by granting special rebates, allowances, discounts and other forms of price reductions, direct or indirect, to some warehouse distributors over and above those made available by respondent to other warehouse distributors who compete with the favored warehouse distributors in the resale of respondent's products. The special price concessions to the favored warehouse distributors are effected by various ways and means, some, but not all, of which are more particularly described as follows:

(a) Respondent grants and has granted "redistribution allowances", varying from 4% to 15.8% to some warehouse distributors on their sales of respondent's products to dealers and users, which allowances are withheld from other warehouse distributors.

PAR. 7. Respondent has been, and now is, discriminating in price in the sale of automotive replacement filters of like grade and quality by granting warehouse distributors special rebates, allowances, discounts and other forms of price reductions, direct or indirect, over and above those made available by respondent to its jobbers who compete with the warehouse distributors in the resale of respondent's automotive replacement filters. The special price concessions to warehouse distributors are effected by various ways and means, some, but not all, of which are more particularly described as follows:

(a) Respondent grants a "warehouse distributor" discount, varying during different periods from 5% to 9%, to warehouse distributors on purchases by them of automotive replacement filters for resale to dealers and users, which discount is withheld by respondent from its jobbers.

(b) Respondent grants "redistribution allowances", varying in total amounts during different periods from 4% to 15.8%, to warehouse distributors on their sales of respondent's products to dealers and users, which allowance is withheld by respondent from its jobbers.

PAR. 8. The special rebates, allowances, discounts and other forms of price reductions granted by respondent, as alleged herein, result, either directly or indirectly, in reducing prices charged such favored purchasers to substantially lower amounts than respondent charges other of its purchasers, many of whom compete with said favored purchasers in the sale of said products of like grade and quality within the trading areas in which they are engaged in business.

PAR. 9. The effect of such discriminations in price, as alleged herein, may be substantially to lessen competition or tend to create a monopoly in the lines of commerce in which respondent and its customers are respectively engaged; or to injure, destroy or prevent competition with respondent or with purchasers therefrom who receive the benefits of such discriminations.

PAR. 10. The aforesaid acts and practices of respondent constitute violations of the provisions of subsection (a) of Section 2 of the Clayton Act, as amended by the Robinson-Patman Act, approved June 19, 1936 (U.S.C. Title 15, Sec. 13).

Mr. Thomas A. Sterner for the Commission.

Willkie, Farr, Gallagher, Walton & Fitz Gibbon, of New York 5, N.Y., for respondent.

INITIAL DECISION BY EARL J. KOLB, HEARING EXAMINER

NOVEMBER 27, 1962

This proceeding is based upon a complaint charging the respondent with violation of Section 2(a) of the Clayton Act and is now before the undersigned hearing examiner for final consideration on the complaint, answer thereto, testimony and other evidence and proposed findings of fact and conclusions of law, together with briefs in support thereof, filed by counsel. The hearing examiner has given consideration to the proposed findings of fact and conclusions of law submitted by both parties and briefs in support thereof, and all findings of fact and conclusions of law proposed by the parties respectively, not hereinafter specifically found or concluded, are herewith rejected, and the hearing examiner having considered the record herein and now being duly advised in the premises makes the following findings of fact, conclusions drawn therefrom, and issues the following order.

1. Respondent, Purolator Products, Inc., is a Delaware corporation with its executive office located at 970 New Brunswick Avenue, Rahway, New Jersey. For many years respondent has been engaged in the manufacture and in the sale and distribution in interstate commerce of many sizes, and types of filters for use in the filtration of fuel, air, oil, water and other liquids and gases. Among the filters so sold and distributed in interstate commerce, were automotive replacement filters, which were sold as replacements for worn components on automobiles, trucks and other motor vehicles. Respondent's net sales of all products for the year 1957, exclusive of the sales of its Canadian subsidiaries, were approximately \$35,880,000. The sales of automotive replacement filters in 1957 were in excess of \$5,000,000.

2. Respondent sells its replacement filters to warehouse distributors located throughout the United States. Such warehouse distributors resell respondent's automotive replacement filters either from a central warehouse location or through branch locations to owners or operators of automotive and truck fleets and to distributors or jobbers, who in turn resell such automotive replacement filters to retailers or dealers

such as service stations, garages and automobile dealers. Many of such warehouse distributors have also resold a substantial portion of their automotive replacement filters purchased from respondent, direct to dealers from their central warehouse locations or through their branch locations.

3. In the sale and distribution of its replacement filters in interstate commerce, respondent has been in substantial competition with other corporations and concerns engaged in the manufacture and in the sale and distribution in interstate commerce of various types of filters for use in automobiles. In general, each warehouse distributor purchasing automotive replacement filters from respondent is in substantial competition with one or more warehouse distributors selling respondent's filters of like grade and quality in the same area. In addition, such warehouse distributor by selling respondent's filters of like grade and quality to dealers and fleets, is in competition with its own jobber customers and with other jobbers purchasing replacement filters of like grade and quality from distributors of respondent.

4. As of March 1, 1960, respondent had 6,956 warehouse distributor-jobber agreements on file. As of August 5, 1960, there were approximately 367 branch locations maintained by such warehouse distributors. The estimated number of dealers purchasing Purolator trademarked automotive replacement filters in the United States was 150,000. In the case of some warehouse distributors with branch locations, sales to independent jobbers were executed by and shipped from the branch locations, as well as from the central warehouse location. Those branch locations may receive respondent's filters from the central warehouse location or by shipment directly from respondent.

5. Warehouse distributors may vary greatly in size. For example, a warehouse distributor may be composed of over ten individual branches located in an equal number of different towns or cities with a central warehouse adjacent to one of the branch locations, or it may have a small central warehouse with one branch, while another warehouse distributor may be a single unit operator with warehouse facilities all at one location, who sells to both jobbers and dealers. Both warehouse distributors and jobbers sell to dealers, typically small retailers who carry little or no stock of automotive replacement parts, and who buy frequently and in small amounts.

6. During the period of January 1, 1957 through February 1, 1959, respondent issued its so-called gray price list showing its net prices to warehouse distributors. In addition, the respondent supplied its warehouse distributors with its blue price list which contained suggested resale prices to jobbers. The respondent also published a second sug-

gested price list (green) for use by distributors and jobbers in selling to dealers. The warehouse distributors prices (gray list) were lower than the suggested net prices to jobbers (blue list), and the suggested net prices to jobbers were less than the suggested net prices to dealers.

7. Effective February 2, 1959, and continuing until the present time, respondent abolished its suggested jobber blue price list. The prices in the gray warehouse distributor price list were increased to levels comparable to those theretofore appearing on the suggested jobber blue price list; and the gray price list thereupon became and has since been a list of respondent's suggested resale prices to jobbers. The prices at which respondent has since sold automotive replacement filters to warehouse distributors, have been uniformly computed by deducting 5% from the suggested gray resale prices to jobbers, either on shipments to the warehouse distributor's central warehouse location or direct shipments to its branch locations.

8. The practices of the respondent involved in this proceeding, consisted of price discriminations arising out of two discounts known as "External Redistribution Discounts" and the "Internal Redistribution Discounts." The entire case-in-chief in support of the complaint was stipulated by the parties and the issues were reduced to three:

- (a) Price Discrimination under Indirect Purchaser Concept.
- (b) Injury to Competition under the Internal Redistribution Discount.
- (c) Meeting a lower price of a Competitor.

I.

External Redistribution Discounts

9. During the period involved in this proceeding, the respondent granted to its warehouse distributors an external redistribution discount either off the face of respondent's invoices or by credit memoranda. Such external redistribution discounts were and are at the following percentages.

February 1, 1957 to January 31, 1958.....	11%
February 1, 1958 to present.....	15%

On some occasions during this period, the respondent granted the external redistribution discount as a percentage of gray prices, rather than the blue prices which showed a difference in the percentages, but in the last analysis, the ultimate net cost of the filters to the warehouse distributor was the same.

10. It has been the announced policy of respondent to pay or allow the above described external redistribution discount only on that

portion of each warehouse distributor's purchases of automotive replacement filters resold by such warehouse distributor from a central warehouse location or through branch locations to jobbers, and since August 3, 1959, to fleets. In order to ascertain the discount due, the warehouse distributor either made a monthly report of all sales to jobbers and fleets upon which discount was paid monthly or the warehouse distributor informed the respondent in writing the percentage of sales which would be made to jobbers and fleets and respondent would then deduct the external redistribution discount from the face of the invoice, or issue a credit memorandum. The reporting warehouse distributor in making his monthly report used forms furnished by respondent which require the sales to be reported on the basis of respondent's suggested resale prices to jobbers.

11. During the period January 1, 1957 through January 31, 1958, respondent did not in all cases adhere to its announced policies concerning the granting of the external redistribution discount described above. For example, in one instance respondent allowed a warehouse distributor the full external redistribution discount off the face of its invoices on automotive replacement filters purchased by it from respondent, and resold directly to dealers (of which respondent had notice). This resulted in said favored warehouse distributor receiving lower net prices, by the amount of the external redistribution discount, than other warehouse distributors, who did not receive said discount, but who purchased automotive replacement filters of like grade and quality from respondent and resold them in the same trade area to dealers in competition with the favored warehouse distributor.

12. The price differentials between warehouse distributors resulting from the granting of the external redistribution discount by respondent to the favored warehouse distributor on automotive replacement filters purchased from respondent and resold to dealers, while not granting such external redistribution discount to competing warehouse distributors on their purchases from respondent of automotive replacement filters of like grade and quality for resale by them to dealers in the same trade area, had a reasonable probability of substantially lessening competition or tending to create a monopoly in the lines of commerce in which such warehouse distributors were engaged, and to injure, destroy or prevent competition with the favored warehouse distributor.

13. The foregoing facts with reference to the external redistribution discounts including injury to competition were incorporated in a stipulation entered into between counsel supporting the complaint and counsel for respondent, and was made a part of the record in this proceeding.

II.

Indirect Purchaser Concept

14. It is the opinion of the hearing examiner and so found that the charges of the complaint based upon the indirect purchaser concept have been sustained. During the years 1949 to 1956, the warehouse distributor contract provided that the distributor distribute Purolator products to jobbers with whom he has executed an agreement approved by the respondent. The agreement with jobbers referred to, provides that the jobber maintain a minimum stock of \$500 of respondent's products, that the distributor will supply jobber at prices shown on blue list (suggested jobber price list); that jobber will purchase his requirements from the distributor and that the agreement between distributor and jobber shall become effective when signed by the parties and recorded by respondent. The so-called recording was simply a signed acceptance of the contract entered into between the distributor and the jobber.

15. From July 1, 1955 to February 1, 1957, respondent executed a letter agreement granting a discount or rebate of 14% upon sales to jobbers with whom the distributor has executed a contract. All such sales to be reported by distributor monthly are based upon the net price shown on blue price sheet. In June 1956, respondent modified its warehouse distributor contract and removed therefrom the provision that distributor's contract with jobbers be approved by respondent. Beginning July 1, 1959, the warehouse distributor's contract with respondent was modified to provide that current price lists were merely suggestive and not intended to be binding in any way.

16. The above actions taken in 1956 and 1959, appear to be an attempt on the part of respondent to divorce itself from the selection of jobbers by warehouse distributors and fixing of resale prices, which the jobber should charge. In actual practice, however, this was not the result. In the memorandum of agreement attached to warehouse distributor's contract allowing an external redistribution discount on sales by warehouse distributors to jobbers, it was expressly stated that such discount would be paid on sales to jobbers who have an executed contract with distributor, known as GS-74, with external redistribution discount based upon suggested jobber price list. This appeared in memorandum agreement in effect during the following periods: February 1957 to February 1958—CX 8; February 1958 to July 1959, CX 9; from July 1, 1959 and subsequent thereto, CX 10(a-b). In jobber agreement forms used from March 1953 through 1956 and later, known as form GS-74, the jobber agreed to purchase his entire

Purolator requirements from the warehouse distributor with which it has entered into this agreement. As set out in the stipulation and as hereinbefore found, respondent issued suggested price lists for sales by the distributor to jobbers and suggested price lists for resale by jobber to dealers. These price lists were generally followed by both the distributor and jobber and, in fact, the external redistribution discount was based upon the suggested jobber price list.

17. As previously found, all the elements necessary to establish that the jobber customer of the warehouse distributor is an indirect purchaser from respondent are present in this record. The respondent has been able to fix and control resale prices by issuance of the suggested jobber price list which were uniformly followed. The respondent has maintained franchise controls and suggests resale prices at all levels down to dealers.

III.

Internal Redistribution Discounts

18. Beginning February 1, 1958, the respondent allowed an additional discount of 4% of the suggested jobber price to its warehouse distributor on all replacement filters reshipped from their central warehouse to their branch locations. This discount was known as the "Internal Redistribution Discount". The single warehouse distributor who makes up the vast majority of the warehouse distributors or customers, does not receive this discount or its equivalent even though it competes with the favored distributor in sales to jobbers, dealers and fleets.

19. Respondent's internal redistribution discount is paid on quantities of its products which the favored warehouse distributor reships from its central warehouse to its branches. Obviously it is available only to those warehouse distributors having branches and who are engaged in supplying their branches from a central warehouse. In 1959 respondent recognized approximately 335 warehouse distributors located throughout the United States. Some of these were owned units of multi-warehouse organizations. Of the total warehouse distributors, approximately 80 had branch locations and were thus physically able to qualify for respondent's internal redistribution discount. Of that number, approximately 70 or 87% were supplying branches from a central warehouse and claimed, and received, the internal redistribution discount. In 1958 respondent paid this discount to 61 of its warehouse distributors.

20. Warehouse distributors may vary greatly in size. For example, Colyear Motor Sales in 1959 had 15 warehouse locations with 24 branch locations, while several competing warehouse distributors are single unit operators with no branches. Both warehouse distributors and job-

bers sell to dealers, typically small retailers who carry little or no stock of automotive replacement parts, and who buy frequently and in small amounts. As a result, warehouse distributors carry large inventories of such parts, very often numbering from 20,000 to 45,000 different items, and jobbers carry somewhat smaller inventories.

21. Automotive parts wholesaling, whether at the warehouse distributor or jobber level, is a keenly competitive business. It is also a business of relatively high costs at all levels just mentioned. As a direct result of such high operating costs, net profit margins typical of the business, range between 3% and 4% (after taxes which are generally considered a cost of doing business). With such net profit margins, both the warehouse distributor's and jobber's profitability are extremely sensitive to the cost of product acquisition. Consequently, the 2% cash discount which is offered by respondent and most other suppliers of automotive replacement parts, is uniformly taken whenever possible, and is considered by warehouse distributors and jobbers alike, to be important, and sometimes essential to a profitable business.

22. Automotive parts and their distribution have been the subject of a long series of recent Commission actions (see for example, *Moog Industries Inc., v. Federal Trade Commission*, 238 F. 2d 43 (1956); *Whitaker Cable Corp. v. Federal Trade Commission*, 239 F. 2d 253 (1956)). In all those cases the capacity of discounts to injure competition has been exhaustively examined. The holdings appear to be unanimous in their evaluation of the relevant economic realities such as the keenness of competition, the very small margins of profits, and the importance of discounts as small as 2% to profitability. For example, *Beard & Stone Electric Co., in Dallas*, which reshipped about 50% of its \$71,237 worth of purchases from respondent in 1959 and was paid \$1,390, had an obvious and substantial competitive advantage which could be used to subsidize its branch operations. The same competitive advantage accrued to *Clinton Square Auto Parts*, which reshipped about 30% of its Purolator purchases and earned \$1,202 in 1959.

23. Although the individual dollar amounts paid favored purchasers by respondent are in themselves substantial in their probable competitive effect, the cumulative result of similar payments by 200-300 other suppliers would have obvious and dramatic anti-competitive effects in this market. These impersonal economic facts hold valid even though unfavored purchasers testify that they have not been injured. *Moog Industries, v. Federal Trade Commission, supra*; *E. Edelman & Co., v. Federal Trade Commission, supra*, 239 F. 2d 152 (1956).

24. Since the filters when delivered become the property of the warehouse distributor, any expense or saving of expense on the part of the customer cannot be used by the seller as a cost justification. This is recognized by the respondent who has maintained upon the record

that the cost studies based upon the internal redistribution discount, were offered solely to show no injury to competition on the theory that redistribution expenses of double handling by the purchaser are equivalent to, or surpass, the allowance given.

25. In support of this contention, respondent presented to the examiner a study made of a group of warehouse distributors by an independent accounting firm, which study purported to show the cost of each of the central warehouse locations in redistributing automotive replacement parts to branch locations, principally by use of the sampling technique. As hereinabove stated, this study was presented not as a cost justification, but for the purpose of supporting respondent's contention that no injury to competition is involved.

26. This cost study was rejected by the hearing examiner as not being relevant and material to the issues in this proceeding. In addition to being based upon customer's costs, the cost study was based upon a sampling technique which was unscientific and valueless. The study purported to be of all automotive parts instead of being limited to automotive replacement filters involved in this proceeding. The record does not show that the samples used were chosen on any other criteria than the arbitrary one of cooperation, with no consideration given to geographical distribution.

27. Respondent's evidence of its customer's costs of doing business cannot be considered competent, relevant or material to the question of competitive injury. The question of competitive advantage or disadvantage is not resolved by determining what a customer does with the price advantage received. Respondent as seller cannot evaluate the relative competitive strength of its customers and vary its prices according to its own determination. Respondent cannot ascertain which of its purchasers is operating at a competitive disadvantage, and, by varying its price, wipe out that "disadvantage." Such pricing could result in the systematic preference of the inefficient customer to the competitive disadvantage of the efficient customer.

28. Respondent's favored warehouse distributors did not initiate the practice of supplying their branches out of a central warehouse location in response to respondent's internal redistribution discount. That method of supplying branches had been in effect for years before the internal redistribution discount came into existence in 1958. The warehouse distributor determined by his own independent business judgment that this method of distribution was the best possible for his operation. As a result of this decision to supply his branches from his central warehouse, the distributor can maintain a smaller inventory at the branch freeing capital for other investment; he can keep his physical facilities small in size at the branch, reducing capital investment and have more control of inventory. The important fact is

that the warehouse distributor had organized and operated his business in a chosen fashion, accepting the competitive advantages and disadvantages inherent in it. The respondent's intervention to pay all or part of the cost of supplying branches has relieved the favored warehouse distributor of an operational cost which has been traditional in his organization.

29. Therefore, it is found that respondent's internal redistribution discount of 4% is paid to the vast majority of its warehouse distributors with branches; that such discounts are substantial in the competitive context of this market; that such discounts are not available to or paid to competing single unit warehouse distributors; and that the discriminations in price resulting from such discounts bestow a substantial competitive advantage on the favored purchasers. Further, it is found that this same discount results in a discrimination in price between the favored warehouse distributor and the jobber with whom he competes for sales to dealers and that such discrimination has the same competitive effect. Likewise, it is found that the discrimination in price of 5% between the favored warehouse distributors and the unfavored jobbers has a similar and added competitive effect.

IV.

Meeting Competitor's Price

30. In an attempted justification of its internal redistribution discount, respondent offered evidence to prove that the lower prices resulting from its adoption of the challenged discount were only a good faith meeting of a lower price of a competitor. That evidence was only the price and discount schedules of two of its competitors. It does not constitute evidence sufficient to support a 2(b) defense for two important reasons. First, the record indicates that prior to February 1, 1958 respondent's price schedule to warehouse distributors was list price less 60%, less 9%, less 11% for sales to independent jobbers. At that time its competitor's prices were 60% less 10% less 10% and 60% less 9% less 10%. Then on February 1, 1958, respondent unilaterally changed its discount schedule to 60% less 5% less 15%. When respondent's competitors did not follow in this change, respondent adopted the internal redistribution discount. From these facts it is obvious that respondent was not meeting a competitor's lower price. Neither of its competitors had lowered its price. Respondent was attempting to repair a defect in the discount schedule it had unilaterally adopted. Section 2(b) is not available on such a set of facts.¹ Second, it is apparent that respondent's internal redistribution discount is designed to accommo-

¹ *Federal Trade Commission v. Staley Mfg. Co.*, 324 U.S. 746 (1945).

date a class of respondent's customers and is applicable to all without regard to any other factors. As such, respondent's discount is simply a system of pricing which results in routine and continuing discrimination in favor of a particular group of its customers. Section 2(b) does not allow a seller to use a sales system which constantly results in his getting more money for like goods from some customers than he does from others.² That defense is reserved for prices which are lowered in response to an individual competitive demand and not as part of a seller's pricing system.³

CONCLUSIONS

1. The price differentials between warehouse distributors resulting from respondent's granting of the external redistribution discount to one warehouse distributor on its purchases from respondent, of automotive replacement filters, which said warehouse distributor resold to dealers while not granting such external redistribution discount to competing warehouse distributors on their purchases from respondent of automotive replacement filters of like grade and quality, for resale by them in the same trade area to dealers, has a reasonable probability of substantially lessening competition or tending to create a monopoly in the lines of commerce in which such warehouse distributors are engaged, or to injure, destroy or prevent competition with the favored warehouse distributors.⁴

2. As heretofore found, the control maintained by the respondent over jobber-customers of its warehouse distributors was such that sales by the warehouse distributors to jobbers should be considered in all essential respects sales by respondent to such jobbers within the meaning of Section 2(a) of the Act, and the granting of an external redistribution discount by the respondent to the warehouse distributor on sales by it to dealers while not allowing such discount or its equivalent to the jobber-customers selling dealers in competition with said distributor has a reasonable probability of substantially lessening competition or tending to create a monopoly in the lines of commerce in which such independent jobbers were engaged, or to injure, destroy or prevent competition by such independent jobbers with said warehouse distributor.⁵

3. The granting of the internal redistribution discount to warehouse distributor-customers having branch locations, while not granting said discount to competing single unit warehouse distributors, had

² *Federal Trade Commission v. Cement Institute*, 333 U.S. 683, 725 (1948).

³ *Standard Motor Products, Inc., v. Federal Trade Commission*, 265 F. 2d 674 (1959), cert. denied, 361 U.S. 826.

⁴ This practice and its effect upon competition was stipulated by the parties and such stipulation was incorporated into the record of this proceeding (Tr. 31-34).

⁵ Effect on and injury to competition was stipulated by the parties (Tr. 34).

a reasonable probability of substantially lessening competition or tending to create a monopoly in the lines of commerce in which such warehouse distributors were engaged, or to injure, destroy or prevent competition with said unfavored warehouse distributors.

4. The acts and practices of the respondent as herein found are in violation of the provisions of subsection (a) of Section 2 of the Clayton Act, as amended by the Robinson-Patman Act.

ORDER

It is ordered, That respondent Purolator Products, Inc., a corporation, and its officers, representatives, agents and employees, directly or through any corporate or other device, in or in connection with the sale, for replacement purposes, of automotive replacement filters, in commerce as "commerce" is defined in the Clayton Act, do forthwith cease and desist from:

Discriminating, directly or indirectly, in the price of such products of like grade and quality:

By selling to any direct or indirect purchaser at net prices higher than the net prices charged to any other purchaser, direct or indirect, who in fact competes with the purchaser paying the higher price in the resale and distribution of respondent's replacement filters.

OPINION OF THE COMMISSION

APRIL 3, 1964

By Dixon, *Commissioner*:

The Commission issued its complaint against respondent, a manufacturer of air, oil, and fuel filters for trucks and automobiles, on March 29, 1960, charging violations of Section 2(a) of the Clayton Act, as amended by the Robinson-Patman Act.¹ The case is presently before us on respondent's exceptions to the hearing examiner's initial decision, dated November 27, 1962, in which the examiner found instances of price discrimination on the part of respondent and issued an order to cease and desist therefrom.

Purolator Products, Inc., hereinafter referred to as respondent, sells its automotive filters in commerce as original equipment for new vehicles and for replacement of worn equipment. This case is concerned with respondent's pricing system in the replacement market or "after-market." According to respondent's executive vice-president, the company enjoys thirty to thirty-two percent of that market, while

¹ 49 Stat. 1526 (1936) ; 15 U.S.C. 13(a) (1958).

AC Spark Plug Division of General Motors Corporation and Fram Corporation hold roughly equivalent shares. It was stipulated that respondent's sales in the replacement market exceeded five million dollars in 1957.

Respondent's only direct sales of its replacement filters are to independent warehouse distributors, most of which handle a multiplicity of other automotive parts. Some of these warehouse distributors operate from a single location, while others maintain central warehouses and reship filters as needed to their owned or controlled warehouse branches. Distributors with branches service customers both from their central location and from their multiple branches. Warehouse distributors resell to jobbers, to dealers (garage owners, filling station operators, and other retail establishments), and to truck fleet operators. Jobber customers of the warehouse distributors also resell to dealers and to fleet operators, and thus are in competition with distributors in such sales. Individual car owners purchase from dealers only.²

The prices at which warehouse distributors purchase respondent's filters are dependent upon the channel through which the filters move to the ultimate consumer. The discount accorded to all warehouse distributors was, at the time of the hearing, sixty percent of the suggested consumer list price, plus five percent.³ The resulting purchase price is thus 38¢ on a hypothetical filter with a suggested consumer price of \$1.00. If the warehouse distributor sells either to a jobber or a fleet operator, he receives an additional fifteen percent "external redistribution discount," which lowers respondent's price to the warehouse distributor to 32¢ ($40¢ - 2¢ - 15\%$ of $40¢$ ($6¢$)). There is no additional discount for sales directly to dealers. Those warehouse distributors maintaining branches are awarded a four percent "internal redistribution discount" on all filters reshipped to their branches from the central warehouse. Thus, the price to the warehouse distributor of a filter sold through one of its branches to a dealer is 36.4¢ ($40¢ - 2¢ - 4\%$ of $40¢$ ($1.6¢$)). If the filter was sold by the branch to a jobber or fleet operator, the warehouse distributor pays only 30.4¢ ($40¢ - 2¢ - 6¢ - 1.6¢$).

When the warehouse distributor sells to a jobber, he sells at respondent's suggested resale price of 40¢, which is computed by allowing

² See Appendix I for diagram of respondent's system of distribution. [Page 43 herein.]

³ In computing its discounts, respondent first deducts sixty percent from the suggested consumer list price. On a hypothetical filter sold to the consumer for \$1.00, the discount amounts to 60¢, and the price of the filter is 40¢. Additional discounts granted to the warehouse distributor are computed as percentages of the 40¢ and subtracted from that amount. The discount of 60% and 5% is thus computed by subtracting sixty percent of \$1.00 from \$1.00, leaving 40¢, and then subtracting five percent of 40¢ from 40¢ ($\$1.00 - 60\%$ of $\$1.00$ ($60¢$)— 5% of $40¢$ ($2¢$)).

a sixty percent discount off the suggested consumer price of \$1.00. When the distributor sells to a dealer, respondent's suggested price entails a 45% discount, making the price 55¢ on the hypothetical \$1.00 filter. Fleet operators now purchase from distributors at the jobber price of 40¢, rather than at dealer prices of 55¢.

Respondent's suggested resale price when jobbers sell to dealers is 55¢—the same as that when distributors sell to dealers. When the jobber sells to a fleet, his price is also the same as that charged by a distributor—40¢. Since the warehouse distributor-jobber price is 40¢, the jobber would thus be selling at cost when he serviced fleets. To provide compensation for the jobber in that situation, respondent grants to the warehouse distributor an additional fifteen percent discount, computed by subtracting fifteen percent of 40¢ from 40¢, on all sales shown to have been made via jobbers to fleet operators. This discount amounts to 6¢ per \$1.00 and is passed on to the jobber by the distributor. Thus, the price to a warehouse distributor for a filter channeled through a jobber to a fleet operator is 26¢ (40¢—2¢—6¢—15% of 40¢ (6¢)).⁴ The warehouse distributor passes the fifteen percent discount to the jobber, who thus pays the distributor 34¢ rather than the normal 40¢ for the filter.⁵

We are presently concerned with price differences in two echelons of respondent's distribution system. First, price differences occur in those instances where warehouse distributors compete with jobbers for sales to dealers and truck fleet operators. The warehouse distributor pays respondent 38¢ for a filter resold to a dealer for 55¢, and thus obtains a 17¢ markup. On the other hand, the jobber purchases filters from the warehouse distributor at respondent's suggested price of 40¢ and resells in competition with the distributor to the dealer for 55¢. The jobber's markup is thus only 15¢. A similar disparity of price occurs when the warehouse distributor competes with the jobber for sales to truck fleet operators. The warehouse distributor pays respondent 32¢ for filters resold to fleets at 40¢, thus receiving a markup of 8¢. The jobber purchases filters from the warehouse distributor at respondent's suggested price of 34¢ and resells to the fleet operator for 40¢, thus receiving a gross profit of only 6¢. In each of the above-mentioned instances, therefore, the jobber is in competition with the warehouse distributor, but realizes 2¢ less on each of its sales of a filter which is eventually sold to the individual car owner for \$1.00.

Secondly, price differences occur as a result of the 4% internal redistribution discount awarded warehouse distributors with branches,

⁴ If the filter is channeled through a warehouse distributor's branch by reshipment, the four percent "internal redistribution discount" is subtracted, making the price of such a filter to the distributor 2¢—4¢. This discount is not passed to the jobber.

⁵ See Appendix II for a chart illustrating respondent's pricing system. [Page 44 herein.]

but withheld from warehouse distributors without branches. The favored warehouse distributor thus pays respondent only 30.4¢ for filters to be resold to fleets and jobbers, while the nonfavored distributors pay 32¢ for filters to be sold to the same customers. The favored distributors pay respondent 36.4¢ for filters to be resold to dealers, while the nonfavored distributors are required to purchase at the higher price of 38¢ when they sell to dealers. This internal redistribution discount not only causes discrimination against those warehouse distributors without branches, but also adversely affects jobbers who compete with the favored warehouse distributors in sales to dealers and fleets. Thus, a warehouse distributor with branches pays respondent 36.4¢ for filters to be resold to dealers, while the jobber pays 40¢ for filters to be similarly resold to the same customers. Since the cost to dealers of these filters is 55¢, the favored warehouse distributors receive profits of 18.6¢, while jobbers receive only 15¢. The favored warehouse distributors pay respondent 30.4¢ for filters resold to fleet operators for 40¢, while jobbers pay the warehouse distributor respondent's suggested resale price of 34¢ for filters similarly resold. Again, there is a 3.6¢ disparity in price on filters sold to the consumer for the hypothetical price of \$1.00. Further, price differences occur as a result of the four percent internal redistribution discount when the filters move through jobbers to fleet operators. The nonfavored warehouse distributors pay respondent 26¢ for filters to be resold to fleet operators via jobbers. The favored distributors pay only 24.4¢. The jobber selling to fleets in competition with the favored warehouse distributor pays respondent's suggested price of 34¢, while the favored distributor selling direct to a fleet pays only 30.4¢. Thus, the internal redistribution discount results in price differences of 1.6¢ between the favored and nonfavored warehouse distributors, and 3.6¢ between the favored distributors and jobbers selling in competition with them.

This case also involves a stipulated violation of Section 2(a) of the amended Clayton Act in connection with the allowance of the fifteen percent external redistribution discount to a single warehouse distributor on goods resold directly to dealers. As previously stated, this discount was generally available only when the distributor sold to jobbers or fleets. The only question regarding this violation is the scope of the order to be issued.

The facts as above stated are undisputed, and the entire case in support of the complaint was submitted on stipulated facts. Respondent urges that the stipulated facts are insufficient to support findings of a violation of Section 2(a) of the amended Clayton Act, and that

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examiner erred in several legal conclusions predicated upon the stipulated facts.

I.

Respondent first asserts that complaint counsel's evidence does not establish the element of competitive injury required for a holding that it violated Section 2(a) of the amended Clayton Act. As previously noted, it is undisputed that price differentials exist throughout the various echelons of respondent's distribution system. A warehouse distributor without branches pays 2¢ less per dollar for filters sold to dealers and fleet operators than does a jobber. A warehouse distributor with branches pays 3.6¢ less per dollar than a jobber for filters similarly sold and 1.6¢ less than a warehouse distributor without branches. It is further undisputed that this differential in price involves purchasers who are in competition with one another.⁶ Thus, there is a clear case of price discrimination. *Federal Trade Commission v. Anheuser-Busch, Inc.*, 363 U.S. 536 (1960).

Complaint counsel relies upon the following paragraphs from the stipulation of facts to establish that the effect of these price differences may be a substantial lessening of competition.

If competent witnesses were duly called by counsel supporting the complaint and duly sworn at the hearings in this proceeding, the competent, relevant and material testimony of such witnesses, plus competent, relevant and material documentary evidence which would be introduced by counsel supporting the complaint and the hearing Examiner would receive in evidence at such hearings, would constitute substantial evidence in support of the following * * * (Tr. 46, 47.)

Automotive parts wholesaling, whether at the warehouse distributor or jobber level, or across such levels (i.e., where the warehouse distributor competes with the jobber for sales to dealers and fleets), is a keenly competitive business. It is also a business of relatively high costs, at all levels just mentioned. As a direct result of such high operating costs, net profit margins typical of the business range between 3% and 4% (after taxes, which are generally considered a cost of doing business). With such net profit margins, both the warehouse distributor's and jobber's profitability is extremely sensitive to the cost of product acquisition. Consequently, the 2% cash discount, which is offered by respondent and most other suppliers of automotive replacement parts is uniformly taken, whenever possible, and is considered by warehouse distributors and jobbers alike to be important, and sometimes essential, to a profitable business. (Tr. 49.)

Respondent assails the latter paragraph as being insufficient to support a finding of competitive injury for the following reasons. First, the exact meanings of such phrases as "keenly competitive," "relatively high operating costs," and "net profit margins" are not apparent

⁶ Tr. 18, 19, 62.

from a reading of the stipulation. Secondly, the paragraph creates a false impression, since filters, as opposed to automotive parts, are not mentioned and there is no statement that the net profit margins of 3% to 4%, which are typical for the industry as a whole, are typical of respondent's customers. Respondent thus intimates that for what appears in the record, the cost of handling filters may be *de minimis* and the profit margins on filters may be munificent. Finally, respondent asserts that the price differentials themselves are insignificant and could have little effect on competition.

In construing the stipulation, we note that it avoided the necessity of calling an endless succession of witnesses to establish contested but pertinent facts, and immeasurably shortened the time spent in hearings. The stipulation was beneficial to all parties concerned and must be interpreted with this factor in mind. We further note that, as a general proposition, stipulations are favored in law. They may be construed liberally and should be interpreted in conjunction with the entire record and the surrounding circumstances. (*National Labor Relations Board v. J. L. Hudson Co.*, 135 F. 2d 380 6th Cir. 1943), *cert. denied*, 320 U.S. 740 (1943); *Hodgson Oil Refining Co. v. United States*, 74 Ct. Claims 303. Any interpretation should if possible, give effect to the intent of the parties. *Cf. United States ex rel. Hoehn v. Shaughnessy*, 175 F. 2d 116 (2d Cir. 1949), *cert. denied*, 338 U.S. 872 (1949).

After considering the instant stipulation in conjunction with the issues in the case, and all surrounding circumstance, we conclude that the phrases attacked by respondent are, in the absence of countervailing evidence, sufficiently clear. Specifically, we conclude that the questioned paragraph of the stipulation does not create an untrue picture by its use of the phrase "automotive parts" rather than "filters." The phrase "automotive parts" when considered in the context of this proceeding must be interpreted to include automotive filters. If the profit on automotive filters is substantially greater than the average profit on all automotive parts, respondent had the opportunity to produce evidence demonstrating such fact. If the statement that the net profit margins ranged between 3% and 4% after taxes was misleading and may not be accorded its generally accepted meaning, or if that margin was not typical of respondent's customers, respondent was accorded ample opportunity to so show. In the absence of any evidence indicating that the questioned paragraph of the stipulation was basically incorrect or created an untrue picture, we are not constrained to strictly interpret it or to endow it with a construction which would rob it of its intended significance. We further note that the phrases under attack are similar or identical to phrases used by this Commission

and the courts in similar cases in summarizing findings of competitive injury.⁷

Respondent's contention that the price differentials themselves are insignificant and thus could not conceivably injure competition is also rejected. When the various price differences are reduced to percentages, their importance within the context of this case is immediately apparent. Thus, the warehouse distributor without branches receives a five percent discount on the purchase price of filters ultimately sold to dealers which the jobber does not receive for similar sales. On sales to fleet operators, the distributor receives approximately a six percent discount on the purchase price not accorded the competing jobber. Viewed in a different light, the two cent differential between warehouse distributors and jobbers on sales to fleets is thirty-three percent of the jobber's gross profit on such sales, while the warehouse distributor's advantage over the jobber on sales to dealers is thirteen percent of the jobber's gross profit. When price differentials of this magnitude occur in an industry characterized by net profit margins of three to four percent, they cannot be construed as inconsequential. An even stronger indication of the potential effect of these discriminations in price is revealed by the stipulated statement that the two percent cash discount offered by respondent and other suppliers of automotive parts is considered by warehouse distributors and jobbers alike to be important and even essential to a profitable business.⁸ On the \$1.00 filter purchased for 32¢ by a distributor for resale to a jobber the two percent cash discount would be six-tenths of one cent. When customers regard a price difference of a fraction of a cent on individual items as vital to a profitable business, it is obvious that the granting on a systematic and continuous basis of a price difference of two cents or more on individual items purchased by the same customers has the requisite capacity and tendency to injure competition.

The four percent internal redistribution discount, which amounts to 1.6¢ per \$1.00 list price and is awarded to warehouse distributors with branches for reshipping filters from their central warehouse to their branches, is similarly capable of causing the requisite competitive

⁷ *E.g., Moog Industries, Inc.*, 51 F.T.C. 931 (1955), *aff'd.*, 238 F. 2d 43 (8th Cir. 1956), *aff'd.*, 355 U.S. 411 (1958); *Whitaker Cable Corp.*, 51 F.T.C. 958 (1955), *aff'd.*, 239 F. 2d 253 (7th Cir. 1956), *cert. denied*, 353 U.S. 938 (1957); *E. Edelman & Co.*, 51 F.T.C. 978 (1955), *aff'd.*, 239 F. 2d 152 (7th Cir. 1956), *cert. denied*, 355 U.S. 941 (1958); *C. E. Niehoff & Co.*, 51 F.T.C. 1114 (1955), *aff'd. as modified*, 241 F. 2d 37 (7th Cir. 1957), vacated with directions to affirm, 355 U.S. 411 (1958); *P. & D. Mfg. Co.*, 52 F.T.C. 1155 (1956), *aff'd.*, 245 F. 2d 281 (7th Cir. 1957), *cert. denied*, 355 U.S. 884 (1957); *P. Sorensen Mfg. Co.*, 52 F.T.C. 1659 (1956), *aff'd.*, 246 F. 2d 687 (D.C. Cir. 1957); *Standard Motor Products, Inc.*, 54 F.T.C. 814 (1957), *aff'd.*, 265 F. 2d 674 (2d Cir. 1959), *cert. denied*, 361 U.S. 826 (1959); *Thompson Products, Inc.*, 55 F.T.C. 1252 (1959); *American Ball Bearing Co.*, 57 F.T.C. 1259 (1960).

⁸ Tr. 49.

injury. On sales directly to dealers, the favored warehouse distributors receive a 4.4% price advantage over their nonfavored competitors. This is 9.4% of the nonfavored distributor's gross profits on such a sale. If the sale is made to a jobber, or directly to a fleet, the favored distributor's advantage over the distributor without branches is 5% on price, and is 20% of the nonfavored distributor's gross profits on the sale. Where the sale is made to a fleet via a jobber, the favored distributor's price advantage is 6%, which again is 20% of the nonfavored distributor's gross profits on the sale. When the favored distributor competes with jobbers for sales to dealers and fleets, its price advantages are 9% and 10%, respectively, amounting to 23% and 60%, respectively, of the jobber's gross profits on the sales. Again, such systematic and continuing price differences cannot be construed to be "*de minimis*" or trivial.

In the context of this case, therefore, where the evidence shows a highly competitive market with narrow profit margins, we conclude that complaint counsel has established through the stipulation a prima facie case of competitive injury, the effect of which "may be substantially to injure competition." *Corn Products Refining Co. v. Federal Trade Commission*, 324 U.S. 726 (1945); *Federal Trade Commission v. Morton Salt Co.*, 334 U.S. 37 (1948); *E. Edelman & Co. v. Federal Trade Commission*, 239 F. 2d 152 (7th Cir. 1956), *cert. denied*, 355 U.S. 941 (1958); *Mueller Co. v. Federal Trade Commission*, 323 F. 2d 44 (7th Cir. 1963); *The American Oil Co. v. Federal Trade Commission*, 325 F. 2d 101 (7th Cir. 1963). If not rebutted, it is our opinion that this showing is sufficient to establish the above-stated requirement of a likelihood of competitive injury. Respondent offered no probative evidence rebutting the prima facie case thus made concerning the price differences in the areas where warehouse distributors compete with jobbers and we accordingly find "* * * what would appear to be obvious, that the competitive opportunities of certain merchants were injured when they had to pay respondent substantially more for their goods than their competitors had to pay." *Federal Trade Commission v. Morton Salt Co.*, *supra*, at pp. 46, 47.

In an effort to show that those warehouse distributors who did not receive the four percent internal redistribution discount for reshipment to branches suffered no competitive injury, respondent offered in evidence studies of central warehouse distributors' costs in reshipping merchandise to their branches. The purpose of these studies was to show that the cost of reshipment to the distributors involved was greater than the amount granted to them by respondent through the redistribution discount and, therefore, that no competitive injury was sustained by the nonfavored warehouse distributors without branches.

Obviously, this is not a cost justification defense under Section 2(a), but is instead an effort to show that there can be no competitive injury because of distributors' added costs in redistributing to branches. Respondent had two of these cost surveys prepared. According to the first, the cost to the warehouse distributors of redistributing the filters to their branches varied between 6.5% and 14.8%, and thus were larger than the 4% internal redistribution discount granted. The second study indicated costs between 4.1% and 12.4%.

The examiner rejected the cost studies, but permitted them to be incorporated in a "rejected" file for further consideration. In so ruling, he reasoned that evidence of buyers' costs was not relevant to the issues in this case, and that the sampling technique utilized in preparing these studies was unscientific and valueless. In reaching our conclusion, we find it unnecessary to consider the sampling technique itself and thus adopt none of the examiner's conclusions concerning the method of preparation of the studies.

The testimony of the representatives of various warehouse distributors called by respondent indicates that warehouse distributors who maintain a central warehouse and reship to branches operate in this manner for reasons of efficiency, convenience, and economy. The branches are in closer proximity to customers and permit the distributors to fill orders more promptly. In addition, distributors realize various savings through maintenance of branches. For example, the branches are able to operate on smaller inventories, since the products can be stored at the central warehouse and then reshipped on short notice. This results in savings of space and permits smaller buildings to be used by the branches. In addition, this method of operation permits a branch unable to purchase in large quantities to take advantage of any savings occurring as the result of mass purchasing. It is further apparent from the testimony that those warehouse distributors who operate branches and reship would not cease to operate in this manner even if respondent's four percent internal redistribution discount were discontinued. Apparently these distributors have determined that they are best able to compete through such organization and thus have freely selected this method of operation. By granting to those distributors who reship to their branches a discount, respondent is, in effect, subsidizing their internal operation. Funds normally used for internal reshipment are released for use elsewhere. Thus, by making available this discount, respondent is granting to the favored distributors a competitive weapon which they would not otherwise receive. We are not of the opinion that such price discrimination may be excused by proof that the buyer receiving the more favorable price has higher internal expenses than his competitor. As the examiner

stated in *C. E. Niehoff & Co.*, 51 F.T.C. 1114 (1955); *aff'd.*, *Federal Trade Commission v. C. E. Niehoff & Co.*, 355 U.S. 411 (1958):

* * * If a price preference can be justified to one customer because the recipient's location is poorer or his rent higher or his maintenance more expensive than those of a customer not receiving such price preference, it would inevitably lead to an evaluation of the efficiencies of hundreds of purchasers and to a probable subsidization by the seller of inefficiency itself. Pricing by resale efficiency must inevitably lead to pricing by customer—the very practice at which the law was aimed to prevent. The Hearing Examiner does not believe such was the Congressional intention. He is of the opinion that the mandate requires only equal price opportunity, that what the purchaser does thereafter in the resale of his own merchandise, if he then operates inefficiently or fritters away his equal price start, is, presently at least, no concern of the law. 51 F.T.C. at 1122.

Accordingly, we conclude that even though respondent's cost studies demonstrate that warehouse distributors spend more in reshipping than respondent granted through its internal redistribution discount for this operation, such fact does not demonstrate an absence of competitive injury. Therefore, the examiner was correct in concluding that the instant cost studies were not relevant to the issue of competitive injury and should be excluded from evidence for that reason.

II.

We next turn to respondent's contention that jobbers who purchase only from warehouse distributors are not "purchasers" from respondent within the purview of Section 2(a) of the Clayton Act as amended and that the price which they pay for products cannot be used as a basis for a finding that respondent has discriminated in price in violation of that Act, which requires a finding that the discrimination in price occurs between different purchasers from the same seller. In past cases, where the evidence has demonstrated that the manufacturer exercised a specified degree of control over the terms of the sale between the wholesaler and his purchaser, there have been findings that the wholesaler's purchaser, termed the "indirect purchaser," was, for the purposes of Section 2(a), a purchaser from the manufacturer. E.g., *Kraft-Phenix Cheese Corp.*, 25 F.T.C. 537 (1937); *Luxor, Ltd.*, 31 F.T.C. 658 (1940); *Dentists' Supply Co. of New York*, 37 F.T.C. 345 (1943); *Champion Spark Plug Co.*, 50 F.T.C. 30 (1953). The courts have recognized and applied this doctrine on several recent occasions. E.g., *Elizabeth Arden, Inc. v. Federal Trade Commission*, 156 F. 2d 132 (2d Cir. 1946), *cert. denied*, 331 U.S. 806 (1947); *I. M. Skinner v. United States Steel Corp.*, 233 F. 2d 762 (5th Cir. 1956); *K. S. Corp. v. Chemstrand Corp.*, 198 F. Supp. 310 (S.D.N.Y. 1961); *American News Co. v. Federal Trade Commission*, 300 F. 2d 104 (2d

Cir. 1962), *cert. denied*, 371 U.S. 824 (1962).⁹ If the doctrine enunciated by these cases is applicable in the present case, the jobbers may be considered "purchasers" from respondent as that term is used in Section 2(a). We thus examine the factors which resulted in such findings in past cases.

In *Kraft-Phenix Cheese Corp., supra*, the Commission found that retailers who received disparate prices on cheese products manufactured by that respondent were purchasers from that respondent within the purview of Section 2(a), even though they had actually received title to the products from independent warehousemen. In arriving at this conclusion, the following factors were considered to be of importance: the exercise of control by that respondent over the channels through which its products were distributed, the respondent's successful and effective establishment of discounts and prices throughout the various levels of the distribution system, and the direct solicitation of the retailers by respondent's salesmen, even though the retailers obtained their title from the independent jobbers. The doctrine was succinctly stated:

* * * A retailer who purchases respondent's goods from jobbers and wholesalers is considered by the Commission to be a "purchaser" within the meaning of the Robinson-Patman Act as well as retailers buying direct. This is because of the fact that respondent recognizes the retailers buying through jobbers as customers by personally soliciting them and by making effective its price policies and schedules as applied to them. A retailer is none the less a purchaser because he buys indirectly if, as here, the manufacturer deals with him directly in promoting the sale of his products and exercises control over the terms upon which he buys. 25 F.T.C. at 546.

In *American News Co. v. Federal Trade Commission, supra*, the latest application of this theory, the court of appeals noted that the indirect purchaser doctrine stemmed from "a fundamental aim of the Robinson-Patman Act to protect buyers' competitors from the evil effects of direct or indirect price discrimination" and commented as follows:

The "customer" or "purchaser" requirement marks one of the outer limits of the seller's responsibility not to discriminate. As long as he exercises control over the terms of a transaction he is held to this duty; otherwise the requirement of the statute could be easily avoided by use of a "dummy" wholesaler. If there is no control the duty naturally ends, for the manufacturer has no power to protect the buyer's competitors. 300 F. 2d at 109-110.

In determining whether a dealer or jobber purchasing a manufacturer's products through a distributor or wholesaler is to be con-

⁹ In *Klein v. Lionel Corp.*, 237 F. 2d 13 (3d Cir. 1956), the court of appeals indicated that the doctrine of the indirect purchaser was inapplicable when the manufacturer established the prices through state fair trade laws. No such issue arises in the instant case, however, because respondent does not utilize fair trade contracts.

sidered a purchaser from the manufacturer, we agree with the court in *K. S. Corp. v. Chemstrand Corp.*, *supra*, when it stated that "each case must be decided on its own facts." We conclude from the above cases that the primary factor in such a finding is that of control by the manufacturer over the prices and other terms of the sale between the intermediary and the indirect purchaser. Where the prices to be charged the indirect purchaser are effectively established by the manufacturer, and where virtually all the conditions and terms upon which the sale is to be consummated are fixed by the manufacturer or are subject to its approval, the predicate for a finding that the indirect purchaser is a purchaser from the manufacturer has been constructed. Other factors to be considered in arriving at that conclusion are instances of direct contact between the indirect purchaser and the manufacturer, such as direct negotiation of franchise agreements, direct solicitation of orders by the manufacturer's salesmen even though the orders are filled by the intermediary and the manufacturer looks to the intermediary for payment, direct negotiations for changes in price, direct policing of the indirect purchaser's resale prices, direct provision of advertising materials, and inspection by the manufacturer to insure that the indirect purchaser is fulfilling the terms of its agreement with the manufacturer's distributor or wholesaler.

In the instant case, the evidence reveals that, from 1949 to the present date, respondent has executed agreements with its warehouse distributors which govern their relationship. The 1949-1956 agreements are typified by respondent's Form GS-84, CX 1, which provided that the distributor would distribute respondent's filters through "Jobbers with whom he has executed agreements approved by the Manufacturer," and/or through the distributor's branch outlets. See also CX 2 (1954 agreement form). In 1956 and 1957, respondent began using a new form which omitted this provision. CX 3, 4. Since 1959, substantially all of respondent's 320 warehouse distributors have signed the current form contract, GS-84B, CX 5, which states that the distributor has the "legal right to select the customers to whom it will sell filters." At the same time, however, respondent began sending its distributors "attachments" to the agreements, in the form of letters. Each letter closes with a request that the addressee sign and return one copy to respondent and attach another copy to the contract the addressee originally signed with respondent. See, e.g., CX 6, 8, 9, 10. These attachments established the redistribution discounts involved here.

The January 1955 letter, CX 6, made available a 10% discount or rebate on "your sales of Purolators * * * at 60% discount when made to jobbers with whom you shall have executed a contract under the

following condition," one of which was that the jobber maintain a \$500 inventory of respondent's products, as provided by "the Jobber Contract, Form GS-74, a supply of which is being forwarded to you." The other condition was that the distributor report sales monthly on respondent's Form GS-77, CX 18, and that "the sales figures reported shall be based on the net price * * * shown on the blue price sheet." See also CX 7 (used from July 1955-February 1957, Tr. 40, 52), to the same effect. In 1957, the 10% discount was raised 1%, and the condition was added that the discount was available only when the jobber was not owned or controlled by the distributor. CX 8, 11. In 1958, the discount was raised to the present 15% figure. CX 9, 12. At that time and since then, respondent's attachments have stated that the allowance of the discount was "subject, however, to the following terms and conditions," one of which has been that the signatory's customers must execute or have executed a Form GS-74 contract. See, e.g., CX 10, 12, 13. See also CX 11.¹⁰

The GS-74 "Warehouse Distributor-Jobber Agreement" has gone through several editions since 1953 when it was first used. See CX 16, 17. They have all required that the jobber purchase his entire Purolater requirements from the warehouse distributor with whom he signs the contract, and that the jobber use Purolater signs and try to promote demand for the product. The revised GS-74, CX 17, mentions price only in a memorandum on the reverse side of the contract, suggesting that the jobber advise respondent of his dealer and jobber price sheet requirements. The earlier version, CX 16, provided "a suggested resale schedule."¹¹

The GS-77 "Report of Sales to Jobbers" form, CX 18, provides spaces for the indication of the name and location of each jobber to whom the distributor has sold respondent's products, and the amount billed to each. The instructions in the margin state that "the sales figures reported shall be based on the net price * * * as shown in the blue price sheet" that respondent supplied. The form also states, "The manufacturer reserves the right to check the information given on this report whenever he wishes to do so." Not all warehouse distributors, however, were required to file these reports. For the "non-reporting warehouses," respondent allowed the jobber discount on the basis of the distributor's representations as to what percentage of his annual Purolater products sales were to jobbers. Respondent reserved

¹⁰ The attachment CX 11 went into use early in 1957, and has the first expressly mandatory language in the clause involving jobber execution of respondent's GS-74 contract, making that a condition of the warehouse distributor's getting the redistribution discount. Compare CX 8 (also adopted early in 1957) and CX 9 (used in 1958), which do not contain expressly mandatory language.

¹¹ It also stated that the distributor would sell to the jobber at the prices shown on respondent's "blue price list."

the right to make periodic record examinations in order to verify these jobber sales volume representations. See CX 11, 12, 13.

The record as a whole thus indicates substantial control by respondent over the relationship between its warehouse distributors and their jobber subvendees, who were nominally the distributor's customers rather than respondent's. As we have indicated, this control by respondent included the approval or selection of jobbers, the imposition of exclusive dealing or full requirements contracts on jobbers, the prescription of distributor-jobber resale prices, and jobber inventory control.

Respondent's executive vice president testified that the provision in CX 1-2 that jobber-distributor agreements be approved was abandoned in 1956 with the adoption of the new form agreement, CX 3. He further explained, but not persuasively, that the real purpose of this provision, and the purpose of the provision that the jobber must buy his entire Purolator requirements from a single warehouse distributor, was to permit respondent, by vertical allocation of customers, to prevent quarrels between its distributors when one tried to raid another's jobbers. Tr. 114, 116, 188-189. Respondent concludes, on the basis of this testimony, that the approval provision was not designed "to limit the activity of the jobber but rather 'to nurture the relationship between our warehouse distributor customers and Purolator.'" Exceptions Br. 18; see Tr. 188. And that at any rate the particular nurturing device has been abandoned since 1956. This explanation misapprehends the significance of the clause and its successors in this proceeding. There is no issue as to respondent's attempting "to limit the activity of the jobber," as if respondent were attempting to make him a mere agent.¹² The relevant issue is whether respondent so limited or controlled the activity of the warehouse distributor in relation to the jobber that the jobber became respondent's customer and the warehouse distributor became virtually respondent's agent in handling the sale. The approval provision, even accepting respondent's witness' explanation, indicates respondent's exercise of substantial control over the distributor-jobber relationship. As for the alleged abandonment of control over the relationship, the subsequent attachments to the contracts imposed as much control as the provisions of CX 3 and CX 5 abandoned, if not more. The first attachments, e.g., CX 8, assumed or implied that the distributors and jobbers must execute respondent's form GS-74 contract before the distributor could receive his functional discount. The later attachments, e.g., CX 13,

¹² Respondent's control over the jobber is relevant only in that it shows that respondent had *so much* control over the distributor-jobber relationship that by this means it could itself exert control over jobbers.

expressly require this. Far from abandoning its control over the distributor-jobber relationship, respondent tightened it by providing and requiring the execution of its distributor-jobber form contract by the two parties.

Respondent denies, further, that it *in fact* exercised control over its distributors' prices to jobbers, so that it can be said to be responsible for whatever competitive injury resulted from them, or over its jobbers' prices to others. It maintains that there is no evidence that it ever attempted to enforce the suggested price provisions. This argument ignores the plain wording of the various attachments, which makes the discount available on the basis of the respondent's suggested resale prices, and which requires the distributor to report sales volumes monthly for each jobber to whom he sells, on a GS-77 form, CX 18, that in turn requires sales to be reported on the basis of the suggested resale prices and that states that the manufacturer may check up on the information given in the report "whenever he wishes to do so." For "non-reporting warehouses" the manufacturer instead periodically examines the distributors' books. See CX 12-13. Further, there is evidence that respondent has policed its jobbers' and dealers' resale prices "to encourage adherence to" the suggested resale price lists. See tr. 44 (stipulation), 199-202 (testimony of respondent's executive vice president). According to respondent, however, it had "absolutely no interest in seeing whether they [suggested prices] are observed or not" and policed them only at the instance of aggrieved jobbers or dealers who complained to it when their competitors failed to observe the price lists.

Finally, respondent denies that it enforced against dealers or jobbers the other contractual obligations it imposed upon them—so that, in effect, it only "suggested" rather than controlled the distributor-jobber relationship. Thus it states that it has not denied discounts to distributors on jobber sales because the jobber failed to keep up a \$500 inventory or failed to sign a form GS-74. This may or may not be, but as of March 1, 1960, respondent had on file some 6,956 GS-74 contracts and over 300 GS-84B contracts with attachments, all of which imposed the indicated contractual obligations on the signatories. In the absence of countervailing evidence, the normal presumption of regularity of conduct, see *Bank of United States v. Dandridge*, 25 U.S. (12 Wheat.) 64, 69-70 (1827), dictates the conclusion that the jobbers and distributors regarded themselves as bound by their contracts. This conclusion is strengthened by respondent's vice president's concession that most jobbers would probably regard themselves as bound by the agreement.

In concluding that the jobbers are to be classified as purchasers from the manufacturer for purposes of Section 2(a) of the Clayton Act as amended, we deem the following factors decisive. First, the respondent possesses the requisite control over the price and the terms of the contract of sale between the distributor and the jobber. As previously noted, respondent's suggested resale prices for this sale are virtually universally adhered to by the distributors. These prices are not established by fair trade contracts. In the overwhelming majority of instances, the respondent provides the contract forms utilized by the distributor in his agreement with the jobber. These contracts require the jobber to purchase his supply of respondent's filters from a particular distributor, and to maintain a minimum inventory. Further, the contract between the distributor and jobber may be disapproved by respondent, and, in any event, must be filed with the respondent. Finally, the degree of control exercised by respondent over the prices which the jobbers pay the distributors is illustrated by the situation which arises when the jobber sells to a fleet operator. As heretofore stated, respondent grants to the distributor a fifteen percent discount which it "suggests" be passed on to the jobber in full on all sales made by the jobber to fleets. There is no indication that jobbers fail to receive this discount. Thus, we conclude that the prices which the distributors charge the jobbers are effectively established by the respondent.

Secondly, we find instances of direct contact between respondent and the indirect purchasing jobbers. Respondent's own salesmen on occasion solicited directly from these jobbers orders which were subsequently turned over to the distributors for processing. Respondent at times "dropped shipped" or shipped direct to the jobbers at the request of distributors. Respondent mailed directly to the jobbers price lists and advertising materials. Respondent's representatives at times "policed" the jobbers to encourage adherence to the suggested resale prices and on other occasions inspected their inventories.

Thus, the evidence reveals that respondent has, in effect, established the prices at which the jobbers purchase from the warehouse distributors and controls the terms under which the purchases are consummated. The evidence also reveals instances of direct contact between respondent and the indirect buying jobbers. On the basis of the entire record, therefore, we conclude that the respondent *did* exercise control over the distributor-jobber relationship to such an extent that the jobbers effectively were respondent's customers rather than the distributors' and, for the purposes of the Robinson-Patman Act, respondent is thus chargeable with the competitive effects of distributors' prices to jobbers.

III.

As a defense to the finding that warehouse distributors and jobbers in competition with each other were charged disparate prices for filters sold to dealers and fleets, respondent contends that the differences are cost justified in accordance with the cost justification proviso of Section 2(a). As applied to filters ultimately resold to dealers, respondent's argument may be summarized as follows. The warehouse distributor pays respondent 32¢ for a filter it sells to a jobber for resale to a dealer. The warehouse distributor pays respondent 38¢ for a filter it resells directly to a dealer. Thus, respondent's "cost" of channeling a filter through a jobber to a dealer is 6¢ more than its "cost" of selling through a warehouse distributor to a dealer. Accordingly, even though the price charged the jobber for acquisition of a filter for resale to a dealer is 40¢ and is thus 2¢ more than that of a warehouse distributor selling in competition to the same dealer, the lower price charged the warehouse distributor is justified by the 6¢ less it "costs" respondent to sell filters through that channel.

We are unable to accept this contention. It is settled that the burden of establishing the cost justification defense rests upon the one claiming its benefits. *Federal Trade Commission v. Morton Salt Co.*, 334 U.S. 37, 45 (1948). The wording of the statute contemplates differences in price related to differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are sold or delivered. In the instant case, the jobber is an indirect purchaser from respondent and pays 40¢ for filters resold to dealers. The warehouse distributor pays only 38¢ for filters it resells to dealers. We have found respondent responsible for establishing this price differential. To justify it under the cost justification defense, respondent must offer evidence showing that its lower price to the warehouse distributor of 38¢ results from lower *costs* of manufacture, sale, or delivery related to differing methods or quantities in which such commodities are sold. The "costs" contemplated under Section 2(a) are vastly different from the "prices" charged by respondent in selling to the various parties.

Here, respondent offered no evidence on the different costs incurred by it in manufacturing, selling, and delivering various quantities of filters to warehouse distributors for sale directly to dealers. Instead, the only evidence before us is the price respondent chooses to charge the distributor—in this instance, 38¢. Moreover, respondent did not establish its costs of selling to a jobber through a distributor. To the contrary, the only evidence we have before us in regard to this latter transaction is respondent's price to the warehouse distributor when

the filter is sold to a jobber for resale to a dealer (32¢), the price at which the distributor sells to the jobber (40¢), and a contention that the 6¢ difference between the 32¢ paid by the distributor when it resells to jobbers and the 38¢ paid by the distributor when it resells directly to a dealer is a "cost" incurred by respondent in channeling filters through a jobber. Without deciding whether the 6¢ may be classified as a "cost" as that term is used in the cost justification proviso, it is obvious that there is no evidence in the record showing either what it costs respondent to distribute to jobbers for resale to dealers or what it costs respondent to distribute to warehouse distributors for direct resale to dealers. Since we have before us only evidence of the prices which respondent chooses to charge rather than evidence of the costs incurred by respondent in the manufacture, sale, and delivery of varying quantities of its products, we have no basis for making a cost comparison and thus are unable to conclude that respondent's different prices are cost justified. Since there was a similar failure of proof in regard to the remaining price differences which respondent contended are cost justified, we are compelled to answer in the same manner. We conclude, therefore, that the differences in prices charged warehouse distributors in competition with jobbers for sales to dealers and fleets are not excused by the cost justification proviso.

Respondent contends that its four percent internal redistribution discount is excused under the Section 2(b) good faith meeting competition defense. Respondent's evidence in support of this defense is confined to a schedule of the discounts and prices of its chief competitors, the resulting comparison which may be made with its schedule of discounts and prices, and testimony by one of its officers that adoption of the discount was necessary. The evidence submitted reveals that prior to February 1, 1958, respondent granted a discount to all warehouse distributors of sixty percent plus nine percent. The effective price of the hypothetical \$1.00 filter to the warehouse distributor was thus 36.4¢ (\$1.00—60% of \$1.00 (60¢)—9% of 40¢). If the filter was in fact sold to a jobber, the distributor received another discount of eleven percent of the price of the filter after the basic discount had been deducted, lowering the warehouse distributor's price to 32¢. This series of discounts was referred to as "60%—9%—11%." Fram Corporation maintained an identical 60%—9%—11% schedule, while General Motors' AC Spark Plug Division used 60%—10%—10%, resulting in a 40¢, 36¢, 32¢ price.

On February 1, 1958, respondent changed its 60%—9%—11% system to 60%—5%—15%. The effect of this change was to raise the price of filters sold to warehouse distributors for resale to dealers from 36.4¢ to 38¢. However, the price to distributors of filters for resale to jobbers

remained at 32¢. The purpose of this change, according to respondent's executive vice president, was to encourage warehouse distributors to sell to jobbers rather than directly to dealers.¹³ Respondent's chief competitors did not alter their prices in this manner. Respondent's vice president stated that this caused "considerable unrest among those warehouse distributors who have branch operations" and that "[t]here was the very distinct risk entailed in the pursuance of this policy that some of these warehouse distributor accounts of ours may see fit to drop our line and take on a competitive line."¹⁴ Respondent thus asserts that the four percent internal redistribution discount granted to those warehouse distributors who reshipped to their branches was granted in good faith response to competition.

We disagree. In the first place, there is substantial evidence indicating that the internal redistribution discount was announced on February 1, 1958, the same date on which prices were raised through a reduction in the basic discount from 60% and 9% to 60% and 5%.¹⁵ If the price changes and discount were announced on the same date, this would indicate that the discount was in fact a preconceived plan of discrimination. As such, it was not excusable under the Section 2(b) defense. Cf. *Exquisite Form Brassiere, Inc.*, Docket No. 6966 (January 20, 1964) [64 F.T.C. 271].

Secondly, and of more importance, respondent's action in granting the four percent internal redistribution discount was not in any manner an individual response to competition. Respondent did not on an individual basis determine which of its customers were receiving or could receive lower prices from competitors and then grant lower prices to these particular customers on an individual basis. Nor did respondent determine which particular customers were likely to defect to competitors because of the availability of lower prices. To the contrary,

¹³ Respondent's executive vice president testified:

"Well our philosophy, as far as the automotive replacement market is concerned, was to emphasize the importance of the warehouse distributor account and to so establish our marketing procedures, marketing policies, as to make our line an attractive line for the warehouse distributor to handle. When we changed from 60, 9 and 11, to 60, 5 and 15, what we were doing was making the line more attractive to the warehouse distributor when he distributed our product line in accordance with our announced policy of distribution, namely, we sell to the warehouse distributor, he in turn sells to a jobber. When he does this, when he distributes the product in accordance with our desired method of distribution, he then qualified for a 15 percent redistribution allowance on the sales that he made to his jobber outlets, his jobber customers.

"We did this in order to emphasize what to us was a very important function in the redistribution of our product. This is the way we wanted it distributed and in order to have it distributed in the manner which we desired, we made this as attractive as we could." (Tr. 92, 93.)

¹⁴ Tr. 98, 99.

¹⁵ E.g., tr. 107. In a statement made by one of respondent's attorneys, which cannot be considered to be evidence, there is some indication that the discount was not announced until later in February of 1958, but was made retroactive to February 1. Tr. 1099.

after receiving some vague threats of defection by a few warehouse distributors with branches, respondent arbitrarily selected and granted to this entire group lower prices through its internal redistribution discount. There is no indication that each member of this group was eligible to receive lower prices from competitors, or that all distributors without branches could not receive lower prices from competitors. In short, respondent's selection of such an arbitrary group for no apparent reason cannot be deemed to be an individual response to competition in any sense of the word. *Federal Trade Commission v. A. E. Staley Mfg. Co.*, 324 U.S. 746 (1945); *Federal Trade Commission v. Cement Institute*, 333 U.S. 683 (1948); *Federal Trade Commission v. National Lead Co.*, 352 U.S. 419 (1957); *Exquisite Form Brassiere, Inc.*, *supra*.

Thirdly, although respondent introduced in evidence its own price lists and price lists of its chief competitors, there is no conclusive evidence indicating that the filters of the competitors sold at the various prices were of the same or substantially the same quality or enjoyed the same or substantially the same public acceptance as those manufactured by respondent and sold at similar prices. Both the courts and the Commission have consistently denied the shelter of the defense to sellers whose product, because of intrinsic superior quality or intense public demand, normally commands a price higher than that usually received by sellers of competitive goods. For example, it has been held that the defense will not lie when the price of Lucky Strike cigarettes is dropped to meet the price level of a "poorer" grade of cigarettes, *Porto Rican American Tobacco Co. v. American Tobacco Co.*, 30 F. 2d 234, 237 (2d Cir. 1929), *cert. denied*, 279 U.S. 858 (1929); or when the price of Budweiser beer is dropped to match the price of "nonpremium" local beers, *Anheuser-Busch, Inc.*, 54 F.T.C. 277 (1957), *set aside for other reasons*, 265 F. 2d 677 (7th Cir. 1959), *rev'd.*, 363 U.S. 536 (1960), *again set aside for other reasons*, 289 F. 2d 835 (7th Cir. 1961). Thus, respondent, by granting virtually identical discounts as those of its chief competitors to a selected class of customers may have been "undercutting" the prices of its competitors and, as a result, not acting in good faith.

It is not disputed that a respondent asserting the good faith meeting competition defense bears the burden of establishing it. *Federal Trade Commission v. Sun Oil Co.*, 371 U.S. 505 (1963). The evidence introduced herein patently falls short of establishing that respondent, in granting the four percent internal discount to a selected group, was granting a lower price "in good faith to meet an equally low price of a competitor * * *."

Respondent advances the additional theory that an essential element in the proof of a "secondary line" injury case under Section 2(a) was

neither alleged nor proved. Respondent asserts that there is nothing to indicate that the favored warehouse distributors who received the internal redistribution discount were "knowing" recipients of a price discrimination, and that such knowledge is an essential element in the offense. In rejecting the contention that knowledge of this nature is a necessary element, we reiterate our conclusion to the same effect in *The American Oil Co.*, Docket No. 8183, 60 F.T.C. 1786 (June 27, 1962), *set aside for other reasons*, *The American Oil Co. v. Federal Trade Commission*, 325 F. 2d 101 (7th Cir. 1963). In that case we pointed out that there is no logical reason why protection of nonfavored customers from the harmful effects of discriminatory practices should be made to depend upon the state of knowledge of the favored customers. Section 2(a) prohibits a price discrimination which may injure competition "with any person who either grants or knowingly receives the benefit of such discrimination, or with customers of either of them." It is our interpretation that the words "customers of either of them" include customers of the person granting the discriminatory price. Under that interpretation, there is thus no requirement that the customer receiving the favorable price be a "knowing" recipient in order for the respondent to be held accountable for its discriminatory actions in charging competing customers higher prices. See H.R. Rep. No. 2951, 74th Cong., 2d Sess., pp. 5-6 (1936).

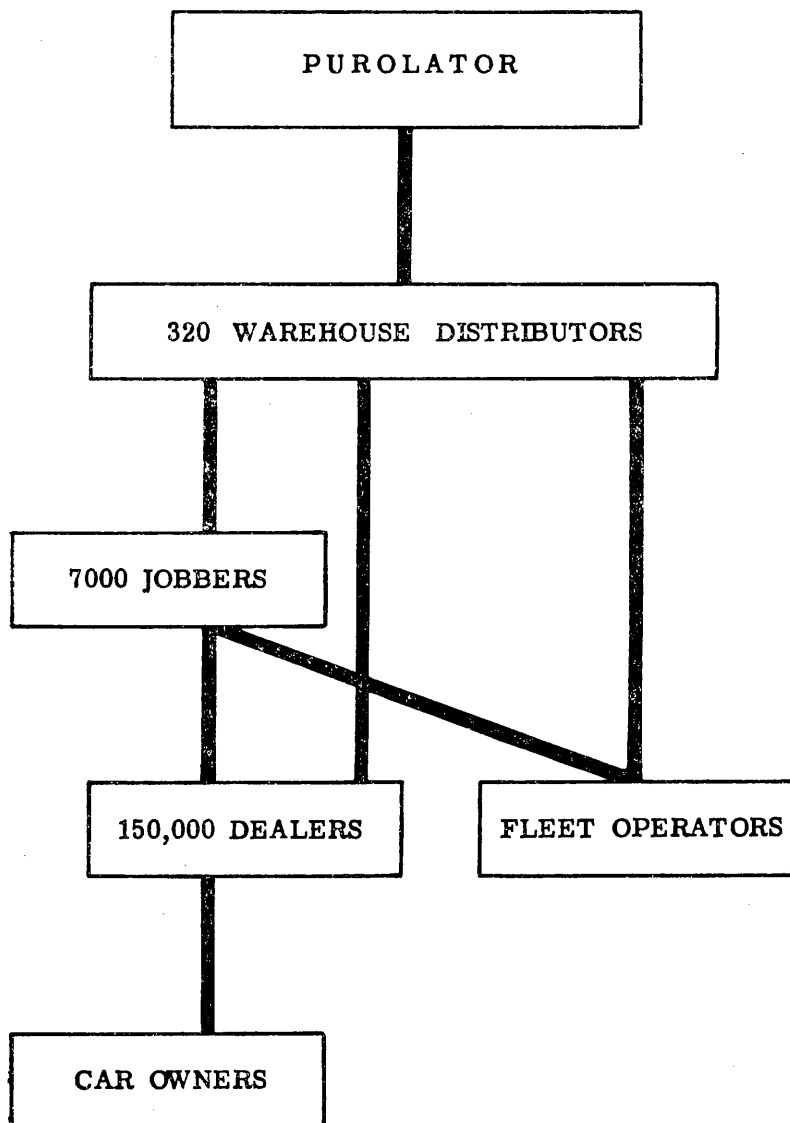
Respondent attacks the order issued by the examiner as being unnecessarily broad. However, respondent has been found guilty of price discriminations in several parts of its distribution system. The violations occurred throughout the country and were pervasive throughout, rather than peripheral to, respondent's business activities. In the circumstances, the public interest calls for a broad order that will block off all paths to violation, rather than merely the traveled ones. See *Federal Trade Commission v. Ruberoid Co.*, 343 U.S. 470 (1952). Such an order, broad though its scope may be, should not be regarded as placing the respondent under a vague, perilous unspecific prohibition. Cf. *United States v. National Dairy Products Corp.*, 372 U.S. 29 (1963). The entry of this order is but the beginning of a relationship under which the Commission is obliged to render the respondent binding and definitive legal advice as to whether proposed conduct meets the requirements of the order. See *Vanity Fair Paper Mills v. Federal Trade Commission*, 311 F. 2d 480, 488 (2d Cir. 1962); *Western Radio Corp.*, Docket No. 7468, 63 F.T.C. 882 (September 25, 1963); *Foremost Dairies, Inc.*, Docket No. 7475, 62 F.T.C. 1344 (May 23, 1963); Rule 3.26, 16 CFR § 3.26. In the circumstances, a broad order is fair to both the respondent and the public.

Respondent also attacks the order for failing to present guide lines which could be used in determining under what circumstances a supplier might grant external redistribution discounts to warehouse distributors on their sales to jobbers having some degree of affiliation or connection with the warehouse distributor. Since this important question was neither precisely raised nor litigated during the hearings, its resolution is not required for the proper disposition of this proceeding. We therefore express no opinion on that issue at this time.

For the aforementioned reasons, an order will issue adopting the order and those parts of the initial decision of the hearing examiner not in conflict with our views as expressed herein. Rules of Practice, § 3.24(b) (August 1, 1963), 28 Fed. Reg. 7080, 7091 (July 11, 1963).

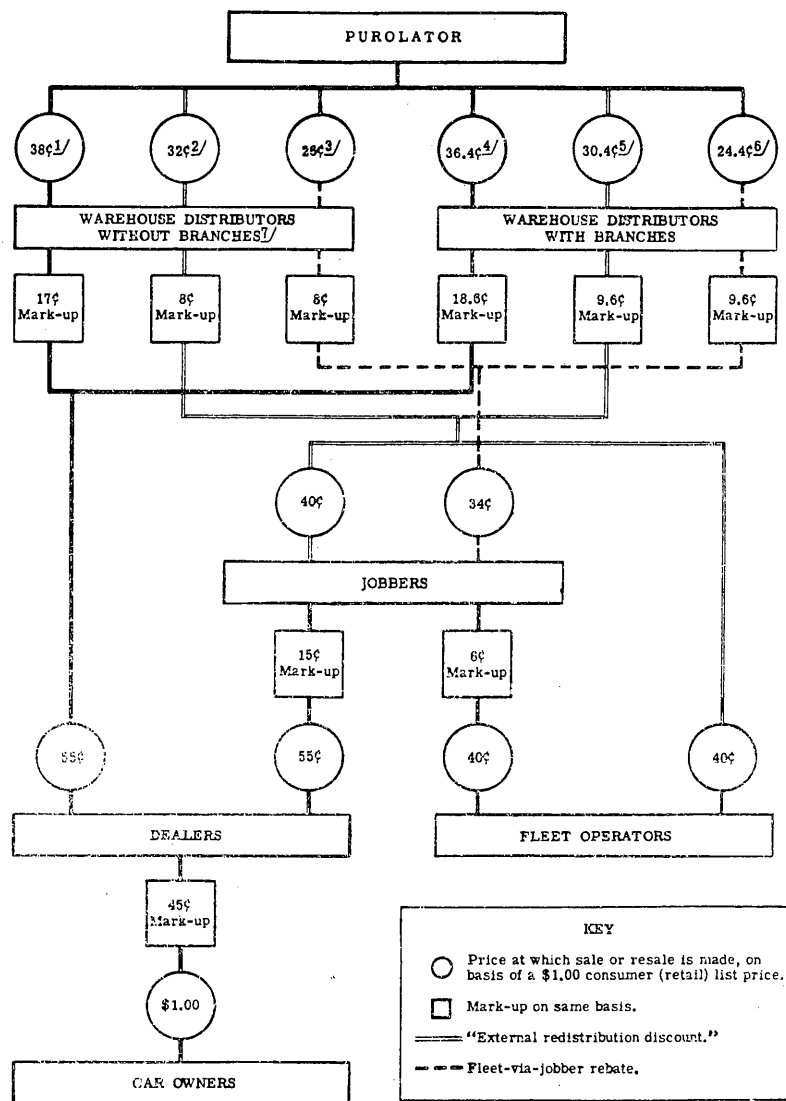
Commissioner Elman does not concur and has filed a separate opinion. Commissioner Reilly did not participate in the decision herein for the reason that he did not hear oral argument.

APPENDIX I
DISTRIBUTION SYSTEM OF RESPONDENT



APPENDIX II

PRICING AND DISCOUNTING SYSTEM OF RESPONDENT



^{1/}Basic discount only.

^{2/}Basic discount and external redistribution discount.

^{3/}Basic discount and fleet-via-jobber discount.

^{4/}Basic discount and internal redistribution discount.

^{5/}Basic discount and external and internal redistribution discounts.

^{6/}Basic discount, internal and external redistribution discounts, and fleet-via-jobber discount.

^{7/}Includes direct shipments to branch locations.

SEPARATE OPINION

APRIL 3, 1964

By Elman, *Commissioner*:

In my opinion in *National Parts Warehouse*, F.T.C. Docket 8039 (Dec. 16, 1963) [63 F.T.C. 1692], I pointed out the complexity of the competing channels of distribution in the automotive parts industry and the resulting danger of easy generalizations concerning the competitive effects of specific methods of distribution. In the present case, this complexity is manifested in the relationships between the different companies within a single channel of distribution. As the chart in Appendix II of the Commission's opinion graphically demonstrates, the "independent" channel of distribution of respondent's products—i.e., through warehouse distributors, jobbers, and dealers—is characterized by an intricate and finely balanced pricing system under which respondent receives different prices for products sold through different sub-channels of distribution, which are defined according to the functions performed by the companies in each of them. The result of this system is that competing companies which perform different functions pay different prices for the same products. It does not necessarily follow, however, that there is present the kind of anti-competitive price discrimination which the Robinson-Patman Act was intended to, or as a practical matter can, prevent.

This system of "competitive-functional pricing", far from being the unique invention of the respondent, is typical of the automotive parts industry. See Davisson, *The Marketing of Automotive Parts* (1954), chapter 24, pp. 909 *et seq.* Moreover, it is a result not of coercive force applied by powerful buyers, but, rather, of the manufacturers' problem, which is especially acute in this industry, of providing for the ready availability of their parts through as many channels and sub-channels of distribution as possible. As a recent study of the industry has pointed out:

The parts industry must maintain a massive, costly inventory, which is always undergoing obsolescence and is in constant need of replenishment * * *. The distributors' problem is to have replacement parts immediately available in every corner of the U.S.—and not to go broke in the process. The way it is done baffles outsiders. Lincoln, "The \$7 Billion Aftermarket Gets an Overhaul", *Fortune*, March 1962, pp. 84, 85.

This problem of distribution is the root of the willingness of parts manufacturers to accept different prices to obtain distribution through different channels. The demand for ready availability by dealers (service stations, garages, etc.) is responsible for a substantial inventory burden and a concomitant demand from those shouldering the burden for sufficient margins or mark-ups to compensate for this cost. As a

result, competition in the automotive parts industry tends to be felt at intermediate distribution levels in the form of spread of margins. Manufacturers vie with one another to make warehouse distributors and jobbers more willing to carry their goods by offering them large margins. As Professor Davisson has described it:

individual sellers must strive to price so that satisfactory volume is obtained from each of several channels used * * *. The objective is to provide margins sufficient to assure sales through each of several channels used. *Functional pricing rests on the reasoning that the vendor is "buying distribution" by accepting different nets from accounts which differ in trade status. Op. cit. supra, p. 39.*

At the same time, and offsetting this rivalry among manufacturers to obtain outlets for their products, competition between the companies at each functional level of distribution tends to reduce these margins to a point approaching the average costs of performing the distributional functions. *Id.*, p. 953. In short, the practice whereby varying net receipts are received by a parts manufacturer from different channels of distribution reflects, as it should in a competitive system, the result of the free interplay of market needs and interests.

Illustrating this pricing system, the chart in Appendix II shows that Purolator receives 38¢ for a filter sold to a warehouse distributor without branches for direct resale to a dealer; 36.4¢ for the same filter sold to a warehouse distributor with branches, also for direct resale to a dealer; and 32¢ for the same filter sold to a warehouse distributor without branches for resale, at a price of 40¢, to a jobber. In other words, Purolator is willing to accept 1.6¢ less than its 38¢ price to obtain distribution through warehouse distributors with branches and 6¢ less to obtain distribution through jobbers.

The Commission should hesitate to tamper with this delicately balanced pricing structure in order to improve the competitive position of the warehouse distributors without branches and of the jobbers who purchase from warehouse distributors. Consider how the Commission's order would apply to the examples given above. It would require that the difference between the 38¢ paid by the warehouse distributor without branches, the 36.4¢ paid by such a distributor with branches and the 40¢ paid by the jobber, be eliminated. But whether, as a practical matter, the Commission's order can eliminate all differences in the prices paid by competing sellers, regardless of differences in the functions which they perform, will depend on competitive forces which the Commission can neither predict nor prevent.

Indeed, the order's ultimate effect may be quite different from that which the Commission now anticipates. Thus, the 40¢ now paid by jobbers can be reduced to 38¢ only if Purolator is willing to accept 2¢

less than its present 32¢ price to warehouse distributors without branches for resale to jobbers, or if such warehouse distributors are willing to accept 2¢ less in their mark-up. But if 32¢ is the minimum price that Purolator is willing to accept in order to obtain jobber distribution, and if 8¢ is the minimum that warehouse distributors will accept as a mark-up, Purolator might simply abandon its present pricing system and instead obtain what distribution it could by selling all of its products to warehouse distributors at the same price, regardless of their ultimate destination, and abandoning any control over the resale price of such distributors. Thus, if Purolator should sell its filters to warehouse distributors for 38¢ regardless of their intended destination, and if the warehouse distributors should insist on an 8¢ mark-up, the jobbers would be forced to pay 46¢ for the same part that now costs them 40¢. Although this result clearly would not accomplish the purposes of the Commission's order, it equally clearly would not violate it, since no price discrimination by Purolator would be involved. Similarly, if warehouse distributors with branches are unwilling, or unable because of their costs, to pay the 38¢ price now paid by distributors without branches, and if Purolator is unwilling to lower the price to distributors without branches, the result may be simply to cause Purolator to abandon its distribution through distributors with branches or to cause such distributors to abandon their branch systems.

The conclusion to be drawn from these examples is that where, as in this case, differences in price exist as part of a complex and delicately-poised pricing system which is the result of normal competitive forces and not of simple discrimination coerced by powerful buyers, the Commission should avoid automatic assumptions of competitive injury. We should recognize that the market forces which have shaped the existing system may be expected to continue to operate, regardless of any Commission order, and that such partial intervention into an industry structure may only serve to introduce new and more intractable competitive inequities.

FINAL ORDER

This matter having been heard by the Commission upon respondent's appeal from the hearing examiner's initial decision, dated November 27, 1962, and upon briefs and argument in support thereof and in opposition thereto; and

The Commission having rendered its decision determining that respondent's appeal should be denied and that the initial decision of the examiner should be modified in accordance with the views and for

Complaint

65 F.T.C.

the reasons expressed in the accompanying opinion, and, as so modified, adopted as the decision of the Commission:

It is ordered, That the initial decision, dated November 27, 1962, be modified by striking therefrom paragraphs 26 and 30, and substituting therefor the findings and conclusions of the accompanying opinion.

It is further ordered, That the initial decision, as above modified and as modified by the accompanying opinion be, and it hereby is, adopted as the decision of the Commission.

It is further ordered, That the respondent herein shall, within sixty (60) days after service upon it of this order, file with the Commission a report, in writing, setting forth in detail the manner and form in which it has complied with this order.

Commissioner Elman not concurring and Commissioner Reilly not participating for the reason that he did not hear oral argument.