Group Buying under the Robinson-Patman Act: The Automotive Parts Cases

Robert B. Fleming

University at Buffalo School of Law

Follow this and additional works at: https://digitalcommons.law.buffalo.edu/buffalolawreview

Part of the Antitrust and Trade Regulation Commons

Recommended Citation


Available at: https://digitalcommons.law.buffalo.edu/buffalolawreview/vol7/iss2/3
GROUP BUYING UNDER THE ROBINSON-PATMAN ACT:
THE AUTOMOTIVE PARTS CASES

BY ROBERT B. FLEMING*

Since 1949 the Federal Trade Commission has issued 22 complaints against manufacturers and wholesalers of automotive replacement parts, asserting the illegality of a certain group buying efforts under the Robinson-Patman Act.1 Nearly half of these proceedings were commenced in 1957 alone. Some of these cases have reached the level of Commission decision and court review, but for reasons to be noted, the group buying problem they manifest remains unsettled. This paper may help to overcome one of those reasons by providing a study of the matter. Beyond the immediate needs however, other factors suggest that these cases may provide a fruitful basis for continuing the dialectic of Robinson-Patman, underway now for over 20 years. The cases embody many of the most difficult and controverted aspects of price discrimination, particularly functional discounts. They will likely provide some decisive teaching in the area of buyer responsibility under section 2(f) of the Act. And they present anew the appeal and conflict which inhere in the cooperative "ideal" when viewed against a Robinson-Patman background. Aside from price discrimination, the cases present a nice problem of determining the circumstances under which corporate entity will be respected when it may interfere with statutory regulation. The entity problem will serve as the formal basis for much of the discussion.

It is assumed in the material which follows that the "improvement of ... distributive processes offers one of the broadest opportunities in American economic life today;"2 that the Robinson-Patman Act reflects one stage of the continuing "struggle for the control of distribution;" and that non-legislative efforts offer the only foreseeable hope toward reconciling its inconsistencies.3

I THE CASES AND THE INDUSTRY

Five of the cases referred to above, all involving seller liability under section 2(a) of the Act, have been concluded by court action affirming FTC cease and desist orders; they are Moog, Edelman, Whitaker, Niehoff and P. & D.4 The group

*Associate Professor of Law, University of Buffalo School of Law.

4. Moog Industries, Inc. v. FTC, 238 F.2d 43 (8th Cir. 1956); E. Edelman & Co. v. FTC, 239 F.2d 152 (7th Cir. 1956); Whitaker Cable Corp. v. FTC, 239 F.2d 253 (7th Cir. 1956); C. E. Niehoff & Co. v. FTC, 241 F.2d 37 (7th Cir. 1957); P. & D. Manufacturing Co. v. FTC, 245 F.2d 281 (7th Cir. 1957).
buying problem, although present in each and relevant to decision in part, was not primary nor vigorously contested, and therefore received inadequate attention. Three other seller cases have terminated at earlier stages, again under circumstances which obviated critical analysis of the group problem.\(^5\) Of the other cases under 2(a), five are pending short of initial decision,\(^6\) and one, Standard Motor Products,\(^7\) has just been decided by the Commission. The opinion in that case does deal with the group problem at some length, but only so as to demonstrate the need for further analysis. The remaining eight complaints pending all name buying groups and their members as respondents, and allege illegal inducement and receipt of price concessions under section 2(f) of the Act.\(^8\) Hearings have been commenced in at least two of these cases, and the complaints involved have survived interlocutory appeals based upon the Automatic Canteen case.\(^9\)

Generally it seems that throughout the course of the notably substantial effort indicated,\(^10\) the FTC has been aiming primarily at alleged threats to competition at the second line of commerce, among purchasers for resale to the retail trade.

Altogether, the respondents in the 22 cases have yet to prevail on a significant point, and the group buying concept has been condemned all round. But the decisive stage is yet to come.

From the available “official” materials\(^11\) the buying groups in question emerge in the following form and context.\(^12\) Starting as early as 1936 when the Act was passed but more often some time thereafter, various automotive parts jobbers

---


10. Respondents in some of these cases have questioned the FTC's elaborate efforts in these cases as compared to its relative inactivity against the “giant” car manufacturers. See brief on behalf of E. Edelman & Co. before the FTC, Dkt. No. 5770, p. 28.


12. There may be considerable variation from group to group with respect to facilities, functions performed, etc., Davission, THE MARKETING OF AUTOMOTIVE PARTS 893 (1954).
GROUP BUYING UNDER THE ROBINSON—PATMAN ACT

(wholesalers selling to retailers) gathered into groups to conduct their purchasing on a cooperative basis. Their intention was generally to pool their market power. Price advantages were usually the main initial consideration, but in some instances other benefits may have been primary. Quantity discounts prevailed in the industry, and group aggregation of purchases achieved substantial rewards for member jobbers. Such quantity discounts were most often cumulative in nature and paid in the form of rebates. The buying group, after deducting expenses, paid over such receipts to each member in proportion to his patronage. Purchase orders to sellers could be sent by member jobbers directly or through the group office. Invoicing by the seller was to the group only, which paid the bills and generally eliminated credit and collection problems for the seller. Shipments of parts were usually made by the seller directly to the member jobbers; only to a very limited extent did the group headquarters handle the goods or have warehouse facilities for doing so. There have been no assertions or even suggestions that the cooperative arrangements served to restrain competition among member jobbers; as often as not members of the same group were geographically situated so as not to be in competition. By 1949 the group buying technique had become rather widely used; in the Moog case respondent was shown to have sold to 15 such groups during that year. Rebates obtained by the groups varied from 5 to 20 per cent of purchase price.

In every adjudication to date, the group buying operation so described has been found illegal as discriminating unfairly against ordinary jobbers. The examiner's statement in the Edelman case may be taken as representative: "In reality, this group set-up is a bookkeeping device for obtaining, collecting and remitting the warehouse discount received from respondent on purchases made by jobber members. The latter, in fact, purchase their requirements directly from respondent, receiving close to a 20% better price than if they had bought simply as a lone jobber, instead of as a member of the group. The functional classification as warehouse distributor is basically artificial." As indicated earlier, however, the respondents in all of the concluded cases have been sellers, and they have not strongly contested the validity of the group operations.

Some characteristics of the automotive replacement parts industry should be

14. In Standard Motor Products, Inc., supra note 7, the Commissioner states that 1500 customers were buying through group organizations. This statement is obviously erroneous; see Initial Decision, FTC Dkt. No. 5721, May 29, 1957, p. 4.
15. In 1954 one group was said to have averaged a 12% gain over the preceding six years. Minutes of a meeting held by a group then forming wherein experience of other groups was discussed.
17. E.g., respondent in the Moog case, supra note 4, did not challenge the finding against group discounts before the reviewing court; and in the Edelman case, supra note 4, respondent withdrew its appeal on the group issue.

233
noted here, as found in official materials and other sources.\textsuperscript{18} Many of the independent parts manufacturers are small businesses, and this is the case with the sellers in the proceedings under consideration.\textsuperscript{19} Annual demand on the other hand is very large; something on the order of five billion dollars' worth of replacement parts and accessories are sold each year.\textsuperscript{20} There is great variety in the means by which these parts are distributed, but two patterns predominate: distribution through independent wholesalers to the general repair or retail trade level, and distribution through car manufacturer service programs.\textsuperscript{21} These basic channel patterns each account for about one-half of most of the market.\textsuperscript{22} Another significant channel is provided by mail order houses. The wholesalers and jobbers with which we are primarily concerned exhibit several rather unique characteristics.\textsuperscript{23} They are numerous—some 11,000 in 1948. They are generally small scale operations; average sales in 1948 were about $200,000. Their operating expenses are relatively high. The automotive repair business requires a ready availability of parts at the general repair trade level, yet there is no significant inventory carried at that level. Accordingly, wholesalers provide most of the necessary inventory, and many of their sales are in retail quantities. The distribution of parts is a highly competitive business, within the independent wholesaler channel, and between that channel and the distribution system aligned with the car manufacturers. Not surprisingly, profit margins of the independent wholesalers are quite low; three per cent on sales, before taxes, is not unusual.\textsuperscript{24}

In the independent channel the second line of commerce may include several steps. The seller may employ an intermediate wholesaler who redistributes to regular jobbers; such wholesalers are usually called warehouse distributors. There may also be sub-jobbers between the regular jobbers and the general repair trade. Wholesalers performing dual functions are frequently found at the second line; their functional compensation or discount (i.e., on sales to jobbers by the warehouse distributor who also competes as a jobber) is frequently on a price-by-reported-use basis. Many times however, the discount for such services (selling the jobbers) is merely part of an overall quantity discount, without distinction made as to type of customers sold.\textsuperscript{25} The latter type of pricing, or what may have been intended as such in part, was held to be illegal in the Moog, Whitaker, Niehoff and P. & D. cases, quite aside from any group buying problems. In these cases the respondents did not primarily defend their quantity rebates or the like as being legitimate functional discounts, undoubtedly because they could not do so

\textsuperscript{18} The description of the industry which follows is based largely on DAVISSON, op. cit. supra note 12, supplemented by interviews in the trade.
\textsuperscript{19} E.g., Niehoff's total sales in 1949 were $2,317,000; in the same year Edelman's sales volume was $1,600,000.
\textsuperscript{20} DAVISSON, op. cit. supra note 12, at 70.
\textsuperscript{21} Ibid.
\textsuperscript{22} Ibid.
\textsuperscript{23} The following is based on DAVISSON, op. cit. supra note 12, at 772-75.
\textsuperscript{24} Id. at 829.
\textsuperscript{25} Id. at 932-33.
GROUP BUYING UNDER THE ROBINSON—PATMAN ACT

convincingly. For all that appeared wholesalers performing whatever functions, pure or mixed, could qualify depending only on quantity sold. On this particular issue, the Commission and courts had little difficulty in finding against the respondents.

In the Edelman case the warehouse distributors received a set functional discount (20%) not tied to quantity. This was held to be illegal because there was no pricing by use.26 Again this holding was reached without regard to any group buying problems. Edelman is important here because the Commission did not attack the designated functional discounts as such. Thus the problem of the groups, if viewed in the Edelman context, becomes one of attempted upward integration by cooperating jobbers seeking as a unit the functional classification of warehouse distributor. In Moog and the other cases, the groups were condemned by the company they kept; for who can tell when or if cumulative quantity rebates are compensating for worthwhile services performed or merely reflect unfair discrimination. In an undifferentiated quantity discount situation, the “aggregating” group members tend almost inevitably to appear as the worst offenders, if only because of the long history of abuses along that line. Accordingly, in Standard Motor Products the Commission hardly bothered to distinguish the group problem from the quantity discount issue; “The group buying program . . . with its system of retroactive aggregate rebates has now been declared to be illegal.”27 (emphasis added)

Moog and the others did in fact wage forcful defenses on other issues, however, especially that of finding the requisite injury to competition. On that point they were eventually overcome by the combined force of the substantial evidence rule and the Morton Salt case.28 Other issues presented were “like grade and quality” and “meeting competition.” Only Niehoff attempted to establish cost justifications for their discounts.

After some consideration of cooperative buying generally, immediately below, attention will be directed to the point of whether buying groups may qualify for such functional discounts as were involved in Edelman. Such a classification was found there to be basically artificial, but the appeal on this point was withdrawn from the reviewing court.

II Group Buying in the Past

The history of Robinson-Patman Act enforcement shows many instances of group buying efforts. For present purposes it will be sufficient to discuss a few of the problems raised heretofore.

27. Supra note 7, at p. 36, 485.
Section 4 of the Act states an exemption for cooperatives which could be construed to protect the auto parts groups.\(^{29}\) While the exemption may be susceptible of such an interpretation, it will not be relied upon here or discussed extensively for several reasons. It would appear that the exemption has been almost completely ignored in the past since the annotations reveal only two cases raising the point.\(^{30}\) Only one of these, Quality Bakers, is pertinent here and will be discussed below. Further, there are doubts about the coverage of section 4. One authority states flatly that the exemption is available only to agricultural cooperatives.\(^{31}\) In addition state laws relating to cooperatives may prevent the auto parts groups from qualifying under section 4. Relatedly, the present structure of the groups may bar qualification as "associations," because most of them are incorporated.\(^{32}\) Lastly, the intent of Congress may have been to exclude from coverage cooperating wholesalers, as distinguished from producers and consumers.\(^{33}\)

Two important cases involving cooperatives in the grocery business should be considered at this point. In the Red & White\(^{34}\) and IGA\(^{35}\) cases, the court affirmed FTC orders against wholesalers and allied retailers engaged in cooperative purchasing. The operations in question were not dissimilar to the auto group schemes. Illegality however was based upon section 2(c) of the Act, the illegal brokerage section, which prohibits receipt of brokerage fees in certain instances.\(^{36}\) Section 2(a) was not involved and the cooperative exemption was not raised.

---

29. Section 4, 49 Stat. 1528 (1936), 15 U.S.C. §13b (1951), provides: Nothing in this Act shall prevent a cooperative association from returning to its members, producers, or consumers the whole, or any part of, the net earnings or surplus resulting from its trading operations, in proportion to their purchases or sales from, to, or through the association.

30. Quality Bakers of America v. FTC, 114 F.2d 393 (1st Cir. 1940); Lane Distributors, Inc. v. Tilton, 81 A.2d 786 (N.J. Sup. Ct. 1951).


32. Ibid. One of the groups presently under attack is organized as a Massachusetts trust, the Six-States group in Hunt-Marquardt, Inc., supra note 8.


34. Modern Marketing Service, Inc. v. FTC, 149 F.2d 970 (7th Cir. 1945).

35. Independent Grocers Alliance Distributing Co. v. FTC, 203 F.2d 941 (7th Cir. 1953).

36. Section 2(c), 49 Stat. 1526 (1936), 15 U.S.C. §13 (1951), provides: That it shall be unlawful for any person engaged in commerce, in the course of such commerce, to pay or grant, or to receive or accept, anything of value as a commission, brokerage, or other compensation, or any allowance or discount in lieu thereof, except for services rendered in connection with the sale or purchase of goods, wares, or merchandise, either to the other party to such transaction or to an agent, representative, or other intermediary therein where such intermediary is acting in fact for, or in behalf, or is subject to the direct or indirect control, of any party to such transaction other than the person by whom such compensation is so granted or paid.
GROUP BUYING UNDER THE ROBINSON—PATMAN ACT

Section 2(c) had already been construed in a strong line of cases\(^{37}\) to preclude receipt of brokerage whenever the intermediary was acting for or under the control of the buyer, rather than the seller paying the fees. This rule obtained no matter what services were actually performed by the intermediary.\(^{38}\) In the grocery cases therefore, the court had little difficulty in deciding that the cooperative intermediary was buyer-controlled, by its members. The important point to note is that no brokerage allowances are involved in automotive parts distribution, and the inflexible rules of section 2(c) are not applicable; analysis is not foreclosed.

The *Quality Bakers* case raised much the same issues as the grocery cases, but with one addition. The buying organization relied upon the section 4 exemption of cooperatives as a defense. Again in the restrictive context of a section 2(c) case, the court found the buying operation unlawful. The court did not decide whether the buying group qualified as a “cooperative association” under section 4. The holding was simply that the exemption did not authorize even qualified associations to engage in practices forbidden by 2(c). Whatever the merits of this decision, \(^{39}\) the brokerage section again foreclosed any analysis of the corporate entity issue that might have been helpful here.

III. THE CORPORATE ENTITY V. ROBINSON-PATMAN

In the course of the earlier discussion of the *Edelman* case, the suggestion was ventured that the auto parts groups might seek legitimacy by having their corporate organizations, considered as business entities distinct from their shareholder-members, achieve functional classification as warehouse distributors. The alternative of considering member jobbers as being somehow individually integrated, does not make good sense. Nor are the legal possibilities enhanced; quite the contrary. The corporate entity notion, besides furnishing a vehicle for discussion, may offer an acceptable tool to facilitate a favorable conclusion. In addition, one attempt has already been made to base a defense upon corporate separateness, in *Standard Motor Products*,\(^ {40}\) and more can be expected.

A THE ENTITY POSSIBILITIES

1. *The Legal background.*

The usual phrases encountered when resolving a conflict between the corporate entity and statutory regulation are familiar enough: evasion or avoidance, a

\(^{37}\) E.g., Oliver Brothers, Inc. v. FTC, 102 F.2d 763 (4th Cir. 1939).

\(^{38}\) Webb-Crawford Co. v. FTC, 109 F.2d 268 (5th Cir. 1940), cert. denied 310 U. S. 638 (1940).


\(^{40}\) *Supra* note 7.
mere screen, a sham, an abuse of the privilege, and the like. The Commission in order to disregard the entity in *Standard Motor Products* may perhaps have relied upon the key factor which should bear in our consideration, the intent of the statute, which may also be taken to include the simple necessities of the situation.\(^{41}\) Other factors to be considered are the intent of the parties and, of lesser importance, the general acceptance of the statute.

Taking the intent of the parties first, this issue may also include the concepts of good faith, of preferring substance to form, and necessity of appraising the equities involved. A leading case is *U. S. v. Milwaukee Transit Co.*\(^ {42}\) It is especially pertinent here, because it involved discrimination in railroad rates under an anti-discrimination statute. Before passage of the law, the shipper involved had been receiving unfair rebates of the very sort that Congress intended to eliminate. When the statute became effective, the shipper immediately organized a dummy corporation which purported to act as a soliciting agent, but in fact allowed the shipper to continue receiving rebates. The court found that the intent of the parties was to evade the law, because of the time sequence, a convincing lack of substance in the subsidiary and a complete identity of interests and personnel. Good faith effort was not evident, nor did any equities favor the arrangement; accordingly, the court disregarded the entity to find a violation of the statute. Some significant differences between this situation and that of the automotive groups will be discussed below.

In regard to the factor of intent of the regulatory statute, a case cited by the Commission in *Standard Motor Products* provides a helpful example. In *Corn Products Refining Co. v. Benson, Secretary*,\(^ {43}\) the issue was whether contracts to sell to a wholly owned subsidiary were hedging operations so as to be valid under the statute involved. The court disregarded the entity to hold that the arrangements did not qualify as hedging. The intent of the statute was clear; hedging essentially involves a shift in risk of loss. Since profit or loss achieved by the subsidiary would accrue in any event to the parent, in the view of the court, the requirements of the statute were not met. Essentially the court decided that the existence of a separate entity will not be permitted to frustrate the purpose of a federal regulatory statute. Good faith and substance were not considered. In the words of another case, "Courts simply will not let interposition of corporate entity or action prevent a judgment otherwise required."\(^ {44}\) In our cases on the other hand the intent of the statute is far from being so clear, and the very matter at issue is whether an adverse judgment is "otherwise required."

The third and less significant entity factor may perhaps be illustrated by a

\(^{41}\) *Id.* at pp. 36, 485-86.
\(^{42}\) 142 Fed. 247 (C.C.E.D. Wis. 1905).
\(^{43}\) 232 F.2d 554 (2d Cir. 1956).
\(^{44}\) In re Clarke's Will, 204 Minn. 574, 284 N.W. 876, 878 (1939).
well known usury case, *Jenkins v. Moyse*. In that case a prospective borrower, willing to pay more than the allowable rate of interest, formed a one-man corporation, transferred to it the property intended as security, and the corporation in turn gave a mortgage on the property to the lender at the rate of interest agreed upon. In foreclosure proceedings, the lender prevailed upon the court to apply the usual rule that the usury defense was not available to a corporation. This refusal to look beyond the corporate form to perceive an "evasion" of the law has been attributed in part to the lack of a strong approval and general acceptance of the usury regulation. In considering the group buyers at hand, therefore, it is possible that the ultimate decision may be favorably affected by the ambivalent character—often reflected in judicial opinions—of the Robinson-Patman Act in relation to the antitrust laws generally. This factor could be enhanced by the presence of the cooperative principle, if that concept still retains much of its sympathetic appeal.

Recent Robinson-Patman entity cases add little in the way of useful analysis. In one case Sylvania Electric Products, Inc., sold television tubes to the Philco Corporation at lower prices than it charged its own distributors. Philco sold these tubes to distributors, one of which was a wholly owned subsidiary, Philco Distributors, Inc. The FTC held Philco and its subsidiary to be one, despite a showing that the latter had a separate administrative, sales and accounting organization. By disregarding the entity, prices to the Sylvania distributors and to Philco Corporation could be directly compared, and a violation of the Act was found. But in a more recent decision, *Baim & Blank, Inc. v. Philco Corp.*, Philco and the same distributor-subsidiary were held to be separate. In the latter case the plaintiff-retailer bought Philco products from the subsidiary, while a competing retailer purchased directly from the parent, at allegedly better prices. Plaintiff's treble damage action under section 2(a) of the Act was dismissed, because he could not show that the differing prices were charged by a common seller. This result obtained despite a showing that, with one exception, the officers of the distributor were also officers of Philco Corporation. The court and perhaps the plaintiff as well apparently treated the issue as if public law considerations were involved, applying the so-called alter ego test.

Neither of the Philco decisions seems helpful for present purposes. Most likely however, *Sylvania* indicates the attitude the Commission will take when faced with the auto parts groups, as they did in the *Standard Motor Products* orders.
case. The *Bairn* case on the other hand, just might indicate that the courts would be susceptible to arguments which convey the suggestion that entity problems are not peculiarly within the expertise of the FTC.

2. The *auto parts groups as factual entities.*

The "intent of the parties" factor as an element of entity problem analysis was mentioned earlier in connection with the *Milwaukee Transit case.* The intent factor as exhibited in the auto parts groups may best be explored by further consideration of the facts. Concerning the inception of the groups, there can be no convincing showing of lack of good faith such as would be indicated by a change of form only, contemporaneous with passage of the Act. It simply did not happen that way. In addition the motives of the group members cannot be described as predatory or aggressive. The quantity discount system prevailing in the industry invited, and competitive pressures made almost imperative, some sort of cooperative defensive efforts. FTC attorneys have consistently argued this point to demonstrate the threat to competition posed by quantity-pricing practices, which, they say, brought on the formation of the groups. Lack of an intent to evade is also shown by the substantial quality of the group organizations. Whatever the records may show as of 1949, present day groups are frequently rather considerable enterprises. They have full-time salaried personnel and adequate capital; nor infrequently they own and operate a warehouse and physically handle more than token amounts of the parts purchased by member jobbers. Such parts are owned and insured by the groups. Further, they perform very real services of considerable benefit to the members. As between members the central unit deals effectively with the problem of obsolescent stocks and overstocking. Not only is quality of purchasing improved, but members are of course simply relieved of a significant portion of their individual purchasing chores, an important matter in

50. But cf., Warren Petroleum Corp., FTC Dkt. No. 6227. In this proceeding the examiner held that 51% ownership of a wholesaler by a supplier was not enough to make the supplier responsible under Section 3 of the Robinson-Patman Act for price cutting by the wholesaler. See Initial decision, 3 CCH Trade Reg. Rep. f125,857, February 10, 1956, affirmed without consideration of this issue, 926,218, September 17, 1956.

51. *Supra* note 42.

52. Interviews in the trade indicated that competitive pressure from several directions was involved; large wholesalers with many branches, mail order houses, and especially car dealers. The large wholesalers, dual-function or otherwise, fare well of course in a quantity discount situation. Car dealers buy from vehicle manufacturers who in turn buy to some extent from sellers such as Moog, Edelman, et al. Vehicle manufacturers buy for two purposes, original equipment and replacement. The danger of course is present, and apprehended in the trade and by the FTC, that the vehicle manufacturers may distribute parts purchased at very low "original equipment" prices to car dealers at prices low enough to hurt independent automotive wholesalers. See, e.g., Champion Spark Plug Co., FTC Dkt. No. 3977 (July 10, 1953).

53. Briefs on behalf of FTC; Moog, pp. 26, 27; Edelman, p. 33; Whitaker, p. 16.

54. No buying group provides its members with all the lines or types of parts the members typically handle.
this industry. And the centralized payment for goods and assumption of the overall
credit risk signifies the substantial financial responsibility of the group enterprises.

In regard to the equities raised by the group buying arrangements, there is
no evidence to date that admission to the groups is unfairly restricted; reliable
figures are not available to suggest the usual amount of investment required of
jobbers upon joining groups, but there have been no assertions that membership
is so expensive that many deserving prospects are excluded. Affirmatively, the
appeal of the cooperative concept, with its implications of preserving small busi-
ness, is helpful, especially in this industry where the very large automobile com-
panies play such an important role.

Considering the factors so far discussed, the auto parts groups can raise some
fairly strong and appealing arguments toward allowing their shareholders to repose
in decent modesty. But the last and probably decisive factor, which was termed
statutory intent in the earlier discussion of the hedging case, remains to be
considered.

B THE REGULATORY STATUTE

Continuing in terms of the analysis employed earlier, the issue becomes:
must the courts simply ignore the corporate entity of the buying groups, because
the Robinson-Patman Act "requires" such a judgment. May the jobbers coopera-
tively integrate upwards one step to the status of warehouse distributors. Accordingly, consideration must be given first to the matter of functional discounts
under the Act.

1. Functional discounts.

In 1922 the FTC issued a cease and desist order against the Mennen
Company for failure to grant a wholesaler's functional discount to buying
cooperatives made up of retail druggists. The cooperatives involved operated
much like the present day groups under consideration, except on a larger scale,
and they had done so long enough apparently to claim some prescriptive rights.
The Commission indeed became the prisoner of its critics, for now it is attacking
in the auto parts cases that which it sought to defend in Mennen; even the

55. "Our only point is that considerations of equity cannot be abolished in
the name of effective competition." Dirlam & Kahn, Fair Competition 277
(1954).
56. Apparently only the usual business tests are applied, such as sales
effectiveness and financial responsibility.
57. Interviews in the trade suggest a possible range of $2,000 to $5,000,
depending on the amount of warehousing done by the group.
58. Corn Products Refining Co. v. Benson, Secretary of Agriculture, supra
note 43.
Robinson-Patman Act could hardly have brought about such a reversal. Meanwhile, the critics, *i.e.*, the courts, have also changed considerably since the days of *Gratz* and *Mennen*. The immediate critic in *Mennen* was the 2nd Circuit Court of Appeals, which dispatched the Commission's interpretation of Section 2 of the Clayton Act with impressive vigor. The court's lesson, that the character of a customer's selling (*i.e.*, who does he sell to), not his buying determines his functional classification, was not lost on the Commission. It remains fixed in the minds of some of the Commissioners today. To determine the Mennen customers' function, the court explicitly set aside the corporate entity of the drug cooperatives. The members were simply buying at wholesale and selling at retail; no wonder that any self-respecting seller would decide to treat them as retailers. At any rate the "character of selling only" view became traditional after *Mennen* and remains in contention today. Under this view the integrated buyer cannot be compensated for services performed for or saved the seller, because—as in the brokerage cases—he did not perform them "for" the seller, rather for himself.

The contrary view, that character of buying may be considered, so that integration can be rewarded, prevailed in the Commission by a vote of three to two in the *Doubleday* case. The examiner had excluded evidence offered by the respondent to show that extra discounts afforded three large jobbers were functional, in compensation for services rendered the seller. The Commission reversed, holding that the evidence must be considered. Chairman Howrey's opinion for the majority admirably stated the case for realistic recognition of the "proliferation of modern marketing methods." He noted the many varieties of integration to be found in the distributive phase of our economy. And he demonstrated the unfairness of a rigid legal ban on seller's compensation of valid integrative efforts. In approving of a service-type functional discount, the Commission indicated, however, that careful appraisal would be required in such cases. No subterfuge would

60. *FTC v. Gratz*, 253 U.S. 421 (1920). This case is usually taken to signify the low point in FTC prestige vis-a-vis the courts. This case was relied upon by the court which reversed the FTC *Mennen* decision, note 61 infra.


62. See the dissenting opinion of Commissioner Secrest in *Doubleday & Co.*, FTC Dkt. No. 5897, 3 CCH TRADE REG. REP. 125,634, p. 35,678 (September 2, 1955). The Commissioner also found that Mennen had discontinued treating the cooperatives as wholesalers in order to reach an "understanding" with the regular wholesalers; see note 59 supra at 278.

63. See the opinion of Chairman Howrey in *Doubleday & Co.*, supra note 62, for a discussion of the history of functional discounts after the *Mennen* case, and the cases there cited.

64. Except of course under the restrictive provisions of section 2(d) of the Act, of which more later.


67. After considering the evidence, the Commission held it insufficient as failing to establish any relationship between the discounts and the value of the services rendered.
be tolerated; the buyer must actually perform the functions; and the amount of the
discount must be reasonably related to the expenses assumed by the buyer. The
majority views were substantially in line with the recommendations of the Attorney
General's Committee earlier that year.69 Much of the opinion in fact repeats
verbatim the text of the Committee Report. The dissent of Commissioner Secrest
was to the effect that only the nature of the customer's selling was relevant, the
traditional view. Commissioner Mead, also dissenting, would allow only such
functional discounts as the seller could "cost justify" under the Act.

Five months after Doubleday, however, the Commission raised some doubts
over their new position on functional discounts in the General Foods case.70
Respondent there, in an effort to improve sales, had set up a number of wagon
distributors to sell the product involved directly to certain institutional customers,
with point-of-sale delivery. The wagon distributors were given extra discounts,
beyond those afforded existing wholesalers selling the same customers. Respondent
claimed first that the discounts were payments properly made under section 2(d)
of the Act. The Commission disposed of this point without considering whether
the opportunity to earn similar discounts was available on "proportionally equal"
terms to the competing wholesalers. The Commission held that the services of
the wagon distributors did not qualify under 2(d) because their character
precluded equal availability to all. Even as between wagon distributors, one
would provide more services (by greater efforts to push the product), and
another less, yet all received the same discount. Respondent "was paying for a
certain method of doing business rather than for specific services actually
rendered." Such a reading of 2(d) is usual and perhaps needed in dealing with
the mischief of doubtful advertising allowances, but it does not solve the problem
of functional discounts.

General Foods raised that problem also, asserting that the wagon distributors
were of a different functional class than the wholesalers, because of differences in
their way of selling, and that therefore the discounts were proper functional

69. ATTORNEY GENERAL'S NATIONAL COMMITTEE, REPORT ON THE STUDY OF THE
70. General Foods Corp., FTC Dkt. No. 6018 3 CCH TRADE REG. REP. ¶25,888
(March 1, 1956).
That it shall be unlawful for any person engaged in com-
merce to pay or contract for the payment of anything of
value to or for the benefit of a customer of such person in
the course of such commerce as compensation or in con-
sideration for any services or facilities furnished by or
through such customer in connection with the processing,
handling, sale, or offering for sale of any products or com-
modities manufactured, sold or offered for sale by such per-
son, unless such payment or consideration is available on
proportionally equal terms to all other customers competing
in the distribution of such products or commodities.
discounts. This argument was rejected, because the wagon distributors and the wholesalers did in fact compete in selling the same customers. This decision was not, however, a reversion to the "character of selling only" rule, nor did it express the view that only functional discounts which do not injure competition are valid. General Foods is consistent with Doubleday,72 because the wagon distributors and the wholesalers had the same functional role. They served the same customers, and the wagon distributors saved General Foods nothing by their methods of buying. Valuable services were indeed rendered, but they were sales services only; no upward integration was present to be left unrewarded. And section 2(d), however read, surely calls for equality of treatment under such circumstances; it was prompted by false sales promotion and advertising allowances. The General Foods case does make it clear however, that section 2(d) will never do to validate functional discounts in any case; quite the contrary. The requisite specificity of services could never be established, as an earlier commentator had suggested.73

Assuming then that the Doubleday precedent retains its vitality, the question is whether the present buying groups qualify under it. Applying the tests suggested by Chairman Howrey, an affirmative answer may be offered. First, there is no subterfuge present, as was shown in the earlier entity discussion. The group as a unit is, or at least may be, a substantial and responsible enterprise; evasion cannot be charged. The second test was whether the buyer actually performs the functions for which he seeks compensating discounts; or, in our Edelman context, whether the grouped jobbers perform the functions of a warehouse distributor. An analysis of those functions may provide the answer. The negative argument is of course that the group carries on significantly less physical warehousing of goods than the usual warehouse distributor, so that equivalent discounts are not in order. This notion is apparently the basis for the frequently heard assertion that the groups do not buy on their own account. The argument can be met by mitigation, as well as confession and avoidance. It should be noted that the warehouse distributor does not physically store all of the goods for which he receives sales credit. Drop shipments and the like which go directly to the jobber from the manufacturer are not uncommon in this industry, as in many others. On such purchases by jobbers "through" the distributor, the latter stands in the same posture as the buying group. Neither sells solely from stock in the warehouse.

But there remains a significant difference in proportion of goods stocked, at least for the present. As to goods not warehoused, the groups are not performing one of the important services usually provided by the distributor. But the mere storage of goods is not the critical element of the distributor's function. The


73. Van Cise, Functional Prices, Symposium on the Robinson-Patman Act (CCH 1957).
supplier could store goods at least as cheaply as the distributor. The latter’s really vital role is to assure the supplier adequate representation of the product in the particular market involved. The seller does not simply dispose of goods at a reduced price when he grants functional discounts; he uses the discounts to buy representation.\footnote{74}{The term “representation” as used here has to do with assuring a seller pre-sold accessibility or channels to the real consumers, in our case the units making up the general repair trade. The jobbers who are in demand by sellers have regular customers for the various types of replacement parts (regardless, to a large extent, of who manufactured these parts). Thus the jobber’s custom is what he can “sell” the manufacturer, and he usually does so for but one manufacturer of any line. See \textsc{Davisson, op. cit. supra} note 12, at 910.} The ordinary jobbers actually provide this representation through their relationships with the general repair or retail trade, one step below. The warehouse distributor’s role is to make this facility of “his” jobbers available to the seller. The tasks entailed by this role are, then, contact, cultivation, selling and servicing of jobbers. Suppliers may of course deal directly with the jobbers, and often do, electing to establish the critical relationships directly, and at a cost. If the seller instead relies upon the warehouse distributor to do this for him, the seller saves that cost and compensates the distributor accordingly.

It can fairly be asserted that the buying groups accomplish the representation role of the distributors with whom they seek equivalent classification. A ready stable of jobbers is made available to the seller by the group. Stated perhaps oversimply, the warehouse distributor “holds” his jobber customers by sales solicitation efforts and good service; the group accomplishes the same result by reason of the patronage refund incentive of the cooperative scheme, along with equally good service. So far, the courts have simply ignored this key representation function performed by the groups; \textit{e.g.}, “Except for one monthly billing instead of 9, the operation saves Niehoff nothing.”\footnote{75}{C.E. Niehoff \& Co. v. FTC, \textit{supra} note 4 at p. 40. \textit{Cf.} brief for FTC in that case, p. 39: \textsc{The group organization though it permits no economies in distribution and though it performs no real distributive function is able to obtain a better price . . . .} In accord and equally untenable are the views expressed in Comment, \textit{A Further Look at Functional Discounts}, 54 \textsc{Minn. L. Rev.} 659, 676 (1956), which discusses the \textsc{Moog} case, \textit{supra} note 4.} Such an analysis is untenable.

Other functions usual to a distributor are also carried out by the groups, such as credit and collections, and product adjustment. On these points the group cannot be distinguished from the distributor.

To the extent that the group does less warehousing than the ordinary distributor, the supplier may incur proportionally higher freight and delivery charges. Fairness would seem to require a lesser discount to the group, reflecting this lost saving to the seller. But this could be managed without threatening the group’s
overall role and status as a "distributor;" rather, such a discount variation would demonstrate the integrity of the group operation.\textsuperscript{76}

The adjustment technique just mentioned may also serve to meet a more difficult question. The warehousing performed by distributors is obviously more significant than mere storage. In this industry availability of parts in the field is critical. The supplier not only wants representation or ready active channels, but the units making up those channels must maintain inventories. The inventory load of the industry is carried by all levels except the retail or repair trade. The buying groups, however, to the extent that they stock less goods in their central warehouse, do not assume the inventory function of the ordinary warehouse distributor. This distinction will of course tend to disappear as the groups increase their warehousing. Again a reduction in functional discount to the groups may provide an answer; although difficult problems of appraisal might arise. There is no information available to indicate whether suppliers are reflecting this point by varying discounts between groups and distributors.\textsuperscript{77} Perhaps it would not be surprising to discover that the groups provide better or more secure representation than the usual distributors, thus making up for the lower inventory load assumed. Competition between the two might then lead to equal discounts and also to sharing of the supplier's distribution job.

The third Dowleday test is concerned with the size of the discount, it must be reasonably related to the "expenses assumed by the buyer." If the object of this test is to disqualify pseudo-integration and reward only valid distributive efficiency, we can restate the concept in terms of the seller; the discount must be reasonably related to the expenses saved by the seller. From the viewpoint of a seller, choosing between alternative channels, that is the main consideration. He wants to rid himself of a task he has been doing at some roughly-known given cost. If a group and a distributor both agree to do part of that job for the same price (discount), at a figure attractive to the seller, he may give them each part of the distribution to carry out and will have no reason to vary the discounts between them. The seller is not concerned with variations in the expenses of his two new "distributors." Viewing the third test in terms of the seller may be necessary because the groups do not of course assume the same expenses as warehouse distributors. The groups perform a function worth so much to the seller, but their whole aim is to eliminate some of the warehouse distributor's expenses. It is submitted that savings from such elimination should accrue to them. By this analysis, the groups would again qualify for functional discounts. There is no adequate information available to show the relationship between present group discounts and sellers' savings, but

\textsuperscript{76} Trade interviews revealed that at least one parts supplier now imposes a five per cent penalty for all drop shipments to jobbers, whether the sales are made "through" a group or a warehouse distributor.

\textsuperscript{77} In the Edelman case, supra note 4, they were treated alike.
GROUP BUYING UNDER THE ROBINSON—PATMAN ACT

the limiting factors are evident. Other things being equal, a seller will not choose to deal with a group at a cost higher than if he carried out the distribution himself, or higher than he would have to pay a warehouse distributor. In other words, the seller pays the going rate for distribution, to either the group or the warehouse distributor.

Altogether then, on the overall issue of functional discounts, the auto parts groups would seem to meet the requirements of the law, according to the teaching of the Doubleday case. At least it cannot well be argued that the mere fact of cooperative ownership of the group entities by the jobbers requires those entities to be set aside.

2. Injury to competition.

The view of functional discounts taken by the Commission in Doubleday must necessarily displace another old rule, that functional discounts are valid only if they do not cause "injury to competition," as that concept is contemplated by the Act. This is sometimes thought of as the status theory, as against the service theory of functional discounts seen in the Doubleday case. Validation of the discounts as suggested above will, it is to be hoped, result in competitive pressure at the jobber level, with which the Commission is now concerned, and at the warehouse distributor level as well. Jobbers lacking the patronage refunds of the group members will claim injury. The best answer is provided by the Attorney General's Committee. "Since aggressive competition among variously organized marketing units is essential to generate the pressures toward eliminating waste and better serving the consumer, no distributive pattern should be favored or prejudiced by law."

As to possible inequities, it should be recalled that the auto parts groups are not exclusive clubs; so far as appears, any respectable jobbers are welcome to join or form their own groups, and the initiation fees are probably modest. Further, any proper concern over injury to other jobbers should, in assigning a cause for that injury, recognize the investment costs of member jobbers as a factor diminishing the effect of their price savings.

3. Cost justification.

In the Edelman case the Commission suggested that the respondent "cost justify" the discounts being granted to buying groups, according to the proviso in section 2(a) of the Act. This suggestion of course raises new doubts that the

78. Cf. Note, YALE L. J., supra note 72; and Van Cise, supra note 73.
79. ATTORNEY GENERAL'S NATIONAL COMMITTEE, REPORT, supra note 69 at 208.
Doubleday precedent is still controlling. It is clear that functional discounts can never be fully cost justified; as indicated earlier, the seller buys distribution with these discounts, and in a competitive industry like this one, he pays the going rate. His cost savings act as a limiting factor, but they may be only roughly known or forecast, and in addition other business factors may enter into a choice of distributive channel. The difficulties of cost justification (as contemplated by the Act) of functional discounts was forecast immediately after the law was enacted, and are only aggravated by the nature of the auto parts industry. Without discussion of the Commission's well known hostility toward cost justification attempts, or the possibility that this attitude has been somewhat modified in recent years, it can be fairly assumed that the cost justification proviso will not protect the group discounts in question. The fact that the Doubleday case required only that functional discounts be reasonably related to the expenses assumed by the buyer was not an inadvertence. If cost justification is to be required for group discounts, those discounts will undoubtedly diminish considerably, perhaps to such an extent that group membership will not longer be attractive to jobbers.

4. The buyer's responsibility

Section 2(f) of the Act, stating the conditions of buyer liability, declares it to be "unlawful for any person engaged in commerce in the course of such commerce, knowingly to induce or receive a discrimination in price which is prohibited by this section." As distinguished from the parts suppliers, the auto parts groups and their members can thus only be attacked directly by means of this section, and that is the case with eight of the complaints now pending before the Commission as noted earlier.

If the views expressed here obtain, qualified buying groups in general will incur no liability, because the prices they receive will be lawful. The lawfulness of those prices is the primary concern of this paper and has already been discussed. Aside from that concern the pending cases obviously pose some very difficult problems of applying section 2(f). Perhaps this accounts for their protracted pendency; one of the cases has not yet reached the state of initial decision, nearly ten years after the complaint was issued.

The Canteen case is the only important precedent in this area, and it required the Commission to show that the buyer had knowledge or its equivalent that the price concessions received were unlawful, in order to make out a prima facie case. Of course, what the records will show in the older cases presently pending is questionable; probably little if any warehousing but considerable sub-

81. "In regard to the seller's situation, the trade discount is at best only a broadly generalized reflection of costs." McNair, Marketing Functions and the Robinson-Patman Act, 4 LAW & CONTEMP. PROB. 334, 347 (1937).
82. DAVISSON, op. cit. supra note 12, at 938-41.
83. See notes 8 and 9 supra.
85. ATTORNEY GENERAL'S NATIONAL COMMITTEE, REPORT, supra note 69, at 194-95.
GROUP BUYING UNDER THE ROBINSON—PATMAN ACT

stance in the groups otherwise. The very recent cases may reveal groups that could meet any of the tests discussed above. In the latter event, recalling the extended discussion above, knowledge of illegality will pose quite an obstacle for the Commission. If evidence of lack of cost savings is required of the FTC, many perhaps will view that prospect with pleasure, in light of the history of the cost justification proviso. On the other hand, if the seller's "good faith meeting of competition" defense under section 2(b) is at issue, the corporate entity problem comes right to the fore in determining the knowledge requirement. In Standard Motor Products the Commission asserted that since a supplier in meeting a competitive price in order to sell to a newly formed group obtains new jobber customers, as well as retaining his old ones among the group, his action would be aggressive, and therefore could not meet the requirements of section 2(b). On the same premise of disregarding the entity of the group, the Commission also held that the respondent seller could not have met the equally low price of a competitor, because the net price to each member jobber varied, depending on his patronage refund from the cooperative. Quantity discounts were involved, and under such circumstances, by the Commission's view, neither the seller's price to the members or his competitor's could be determined when the sales were being negotiated. Enough has been stated perhaps to show that these cases pose enough 2(f) problems to indeed require ten years of consideration.

IV CONCLUSIONS

The views offered here if accepted would provide a basis for validation of the group buying technique, under conditions which would not be impossible for cooperatives to meet, and without legislative changes in the Act. The conclusion is not applicable only to the automotive parts industry. Further, it is hoped that these views may provide a more reasoned basis for disposition of the many pending cases than has been evident thus far.

Eventual approval of group buying by the Commission and the courts can hardly be prophesied at this time. The authority of the Doubleday precedent is much too questionable, especially considering the suggestion in Edelman that group discounts be cost justified. Further the sequence of the auto parts cases, decided and pending, will weigh against favorable decision, because of the cumulative quantity discount factor, because the sellers' cases have come up first.

Final disapproval by the authorities would be an unwelcome result. The cooperative buying idea as discussed here surely offers a worthwhile opportunity to vindicate the equitable interests embodied in the Robinson-Patman Act without sacrifice of economic efficiency. One prophecy may be ventured; the buying groups may prove sturdy and attractive enough to survive somehow, no matter what conclusion these cases reach. Red & White, IGA, and the Mennen drug-cooperatives seem still to be with us.

249