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Trade Regulations—Robinson-Patman Act—Justification of a Discount Based upon a Reduced Brokerage.—Thomasville Chair Co. v. FTC.

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very dangers recognized as existing when the insider is the optionee are also present, although admittedly to a somewhat lesser degree, when he chooses to speculate through the writing of these options.

More substantial profits and less risk are perhaps attainable if the insider himself purchases and sells puts and calls, but he may well be subject to the restrictions of section 16(b),[21] which in the light of this decision, he avoids by the issuance of a straddle. In view of the present opinion, the essential thing about the act of exercising the option would seem to be not that the insider has committed himself and cannot withdraw, but rather the mere state of bilateral contractual certainty. It is unfortunate if, in reaching this result, the court was influenced by the contention that Landa had no control over the exercise of the option, and that "far from allowing an insider to indulge in the speculation proscribed by section 16(b), the issuance of a straddle places him in a strait-jacket."[22] Perhaps liability should not be contingent on the exercise of the option when the insider is the optionee and when, for speculative purposes, he has already made, so to speak, his last move by binding himself to a unilateral contract.

In conclusion, given the strict adherence to contract terminology by the court in interpreting the relevant provisions of the act, the Securities and Exchange Commission should adopt remedial regulations under the power given to it in section 9(b),[23] whereby the Commission has the power to adopt rules dealing with all aspects of the use of put and call options. As of this date, however, the Commission has not seen fit to exercise this power.[24] In the long view however, further acceptance of this rigid interpretation will not only severely hamper the effectiveness of the act, but may relegate the Commission to the more unsatisfactory alternative of retrospective response by administrative decree to each new and ingenious speculative scheme.

NORMAN JACOBS

Trade Regulations—Robinson-Patman Act—Justification of a Discount Based upon a Reduced Brokerage.—*Thomasville Chair Co. v. FTC.*[1]—The petitioner brought this action to set aside a cease and desist order of the respondent, the Federal Trade Commission. The order was issued to curb Thomasville's pricing schedule which granted a five per cent discount

[21] Comment, Put and Call Options Under Section 16(b) of the Securities and Exchange Act, 69 Yale L.J. 868, 894 (1960). It is therein suggested that it is "unlikely" that insider option writing will develop into a "widespread" problem. This is no doubt true because the successful issuance of puts and calls requires rather extensive holdings so as to allow the speculator to deal in averages and thus protect himself from any miscalculation. Nevertheless, the relatively smaller profits available to the insider-writer of the option, and even the infrequency of this manner of speculation, in no way requires the result reached in the *Landa* case.

[22] Brief for Appellee, p. 13.

[23] 48 Stat. 889 (1934), 15 U.S.C. § 78i(b) (1958).

[24] 2 CCH Fed. Sec. L. Rep. ¶ 22,621 (1958).

[1] 306 F.2d 541 (5th Cir. 1962).

to the class of customers whose average purchase of furniture on a yearly basis amounted to $50,000 or eight carloads.[2] Sales to this group brought a commission of three per cent to Thomasville salesmen while purchases by another class carried a six per cent commission. The FTC found that in some instances the discount to the former was only possible because of the lower commission and held this to be a violation of Section 2(c) of the Robinson-Patman Act.[3] The Court of Appeals for the Fifth Circuit set aside the order and remanded the matter. HELD: A reduced price resulting in part from a lower commission to the seller's agent is not necessarily illegal, but such lower brokerage must be examined to determine whether it is justifiable. The court stated that a seller's brokerage payment to his agent can be dictated not only by a desire to attain an order by giving a favored customer a reduced price, but also by the legitimate estimation of the proper brokerage appropriate to a classification of customers. While the former is illegal since it is an "ad hoc" discriminatory maneuver, in the latter instance the seller is performing a fair pricing function.[4] A lower charge to a buyer based upon a legitimate reduction of commission is a fair response to the seller's cost.

The theory behind the FTC case is simply that "Section 2(c) makes unlawful petitioner's discriminatory discounts granted to its favored customers in lieu of all or part of the commissions of its sales representatives."[5] This section of the law was passed by Congress to combat the use of brokerage devices for concealment of price discrimination.[6] The wording of the law condemns any payment or discount in lieu of payment of brokerage *between* opposing parties. This especially envisioned the pressure a large buyer would bring against a seller to lower his price by not paying a brokerage fee to his own agent, or allowing the buyer to perform services normally rendered by a broker. Small purchasers incapable of exerting such pressure and unable to provide such services paid a higher price. The large number of cases involving brokerage payments attest to the key purpose of the subsection.[7]

Not clearly covered in the law is the function of commission payments *to one's own agents*. Adjustments of this might seem to be within the cost regulation of a product. Part of the Robinson-Patman bill is a general proscription of discriminatory pricing, subsection (a).[8] Included in this subsection is a proviso allowing a defense based upon demonstrated savings

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[2] The case also presents a factual issue as to determining the cost justification defense on these classifications, id. at 543-44.

[3] 49 Stat. 1526 (1935), 15 U.S.C.A. § 13(c) (1958). Pertinent parts are:

> . . . it shall be unlawful for any person . . . to pay or grant . . . a commission . . . or other compensation, or any allowance or discount in lieu thereof . . . in connection with the sale . . . of goods, wares, or merchandise . . . to the other party to such transaction. . . .

[4] "It thus becomes necessary for the commission to permit a full scale inquiry . . . as to whether the company's long standing contract with its salesmen under which they received a smaller commission for sales to this list of customers could be legally justified." 306 F.2d at 545.

[5] Brief for Respondent, p. 13.

[6] Rowe, Price Discrimination Under the Robinson-Patman Act 331 (1962).

[7] Great Atl. & Pac. Tea Co. v. FTC, 106 F.2d 667 (3d Cir.), cert. denied, 308 U.S. 625 (1939); Oliver Bros. v. FTC, 96 F.2d 687 (2d Cir.), cert. denied, 305 U.S. 634 (1938).

[8] 49 Stat. 1526 (1936), 15 U.S.C.A. § 13 (1958).

which came from methods of production or distribution. Originally, in the Senate version, brokerage was excluded from this defense.[9] Senator Logan, the floor manager of the bill, objected to this exclusion stressing that the bill had in mind only "sham brokerage."[10] In the final version, the express exclusion of brokerage was struck out for a reason subject to alternate interpretations.[11]

Characteristic of the original cases brought under subsection (c) was the absolute, per se impact given to the subsection.[12] It did not matter what form the transfer of brokerage possessed,[13] nor did it matter what services were provided in return.[14] If the courts or the Commission found that a brokerage or discount in lieu thereof had passed from seller to buyer or buyer's agent, then the transaction was void. Always argued and always struck down was the contention that if the brokerage was paid to the buyer because of savings he afforded to the seller—the cost justification defense to subsection (a)—such should be permitted. It has been continuously concluded (even the *Thomasville* court pays homage to this) that the cost justification defense of subsection (a) does not apply to subsection (c).[15]

Not until *FTC v. Henry Broch & Co.*[16] was a discount based on a seller's adjustment of brokerage vis-à-vis his own agent held illegal. Immediately prior to that case something of a chink was found in the armor of the subsection in *Robinson v. Stanley Home Prods., Inc.*[17] This was a suit to recover a lost commission. After dismissing the plaintiff as a salesman, the seller passed the unpaid commission on to the buyer in the form of a lower price. The court upheld the reduction of the price since the seller was free to totally eliminate the salesman and hence reduce his costs.[18]

The crucial decision regarding the illegality of internal brokerage

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[9] S. Rep. No. 1502, 74th Cong., 2d Sess. 5 (1936).

[10] This discussion appears in the Senate hearings on section 2(c). Hearing Before a Subcommittee of the Senate Committee on the Judiciary on S. 4171, 74th Cong., 2d Sess. 52 (1936):

> Witness: When times get dull we make contracts with big manufacturers to take our goods at lower cost . . . . That cost has to come out of our selling cost, and I understand you cannot deduct brokerage.
>
> Senator Logan: You can deduct legitimate brokerage. This sham brokerage is what this bill is aimed at. It is perfectly proper under this bill to pay and deduct legitimate brokerage.

[11] H. R. Rep. No. 2951, 74th Cong., 2d Sess. 6 (1936): "The words 'other than brokerage' which appeared in the Senate amendment are eliminated . . . for the reason that the matter of brokerage is dealt with in a subsequent subsection of the Bill." The majority opinion in FTC v. Henry Broch & Co. 363 U.S. 166, 171 n.8 (1960) states that "The legislative history is barren of any indication that a change in substance was intended." The minority finds just the contrary. 363 U.S. at 186 n.11.

[12] Subsection (c) "prohibition . . . is absolute." Great Atl. & Pac. Tea Co. v. FTC, supra note 7, at 674.

[13] Quality Bakers v. FTC, 114 F.2d 393 (1st Cir. 1941).

[14] Fitch v. Kentucky-Tenn. Light & Power, 136 F.2d 12 (6th Cir. 1943).

[15] "[T]he prohibitions of Section 2(c) are to be read independently . . . ." 306 F.2d at 545.

[16] Supra note 11.

[17] 272 F.2d 601 (1st Cir. 1959).

[18] This ruling was given explicit blessing in the *Broch* case, supra note 11, at 176 n.18.

manipulation must be, excluding the instant case, the *Broch* decision. There, the FTC declared illegal the seller's attempt to lower the commission he paid to his salesman so as to meet a price requested by one special buyer. The Supreme Court overruled the circuit court by holding that the subsection was sufficiently broad to prohibit indirect payment of brokerage. As framed in the FTC ruling, the economic effect is judged to be the same both where a commission is paid directly to the buyer and where the seller's broker is paid a smaller commission, thus enabling the seller to reduce his price to a particular buyer.[19] While it may be apparent that the economic effect is the same, it was not apparent to the Supreme Court that parallel effects produced parallel illegality. The *Broch* Court split five to four on the application of subsection (c) to seller-agent arrangements. The dissenting justices urged that the subsection was not intended to regulate brokerage between seller and seller's agent or buyer and buyer's agent when services are rendered.[20]

The most interesting facet of the decision however, was the bone tossed to commerce in the form of dicta by the majority. In the opinion Mr. Justice Douglas stated that a price reduction following a lowered brokerage fee is not always illegal, but falls under the subsection ". . . only when given to favored customers."[21] "The majority reserved the right to make a different finding on the appropriate facts."[22]

It is this bone which the *Thomasville* court seizes and, so to speak, adds meat when finding a possibility that such facts exist here.[23] The manner of determining justification of reduced brokerage in the case is not so crucial as is the fact that the court clearly and unequivocally states that it may be found. Yet, it is intriguing to notice the process which the court uses. To take the discount based on brokerage out of the prohibition of the law, the court finds that there was no discrimination.[24] It was in the *Broch* case that the Supreme Court first held that "discriminatory pricing" was at the heart of subsection (c).[25] It had previously been held that in subsection (c) violations, discrimination need not be proven.[26] The dissent in the *Broch* decision arguing against the factual distinction presented by the majority restated the irrelevancy of discrimination as a factor in the case, stressing that the decision would lead to the destruction of the independence of subsections (a) and (c).

What *Thomasville* brings out, in accord with *Broch,* is that a discount in lieu of brokerage is not always discriminatory. The *Thomasville* court tells the FTC to find first that the brokerage reduction is unjustifiable, and

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19 Henry Broch & Co., FTC docket No. 6484 (Dec. 10, 1957).

20 363 U.S. at 181.

21 Id. at 176. "A price reduction based upon alleged savings in brokerage is an 'allowance in lieu of brokerage' when given only to favored customers."

22 Id. at 177 n.19. "We need not view this administrative practice as laying down an absolute rule that Section 2(c) is violated by the passing on of savings in broker's commissions to direct buyers . . . ."

23 The case was remanded for rehearing on this principle.

24 306 F.2d at 545.

25 363 U.S. at 177.

26 Biddle Purchasing Co. v. FTC, 96 F.2d 687 (2d Cir. 1938).

only then may it consider whether the discount is a violation of subsection (c).

While the court is not clear as to the guidelines for this new method of determining subsection (c) violations, it still takes pains to avoid the snare of fusing the defense of subsection (a) with subsection (c).[27] The court's position is not as artificial as it may appear. It was argued in the respondent's brief that the mere fact that the conduct in question is nonviolative of subsection (a) does not preclude its violation of subsection (c).[28] Something of the converse may also be true, that if a business practice clearly falls within the sanction of subsection (a) it must so remain and not be invalidated because, in form though not in substance, it is described in subsection (c).[29] With the *Thomasville* decision, it is now necessary to determine whether the brokerage rate was an internal matter—the seller's response to factors not peculiar to one customer—or was a concession to favored customers.[30]

A criticism which can legitimately be brought to bear on the case is that despite all of its fine distinctions there seems, in effect, to be a fusion of subsections (a) and (c), thereby greatly diluting the effect of subsection (c). Whether this unfortunate tendency actually is present will depend on the use of *Thomasville* in future decisions involving subsection (c) violations.[31]

PAUL E. D'HEDOUVILLE

Trade Regulations—Robinson-Patman Act—Meeting Competition.—*Sunshine Biscuits, Inc. v. FTC.*[1]—Sunshine Biscuits manufactures and distributes baked goods on a nation-wide scale, and in the Cleveland area it sells potato chips to independent retail outlets by way of its Velvet-Krun-Chee Division. In 1959 competing local distributors offered discount prices to some of Sunshine's Cleveland customers and Sunshine responded with similar discounts. The lower prices enabled Sunshine to keep its old customers, and were also a source of new business from customers who had not previously purchased from Sunshine. The Federal Trade Commission issued a complaint against Sunshine showing that its discriminatory prices had injured competition as prohibited by Section 2(a) of the Robinson-Patman Act.[2] At a subsequent hearing the examiner found the Commission's

[27] Rowe, supra note 6.

[28] Brief for Respondent, p. 24.

[29] 80 Cong. Rec. 9417 (1936): "There is no limit to the phases of production, sale and distribution in which such improvements may be devised . . . nor from which those [improvements] . . . when demonstrated may be expressed in price differentials in favor of the particular customers whose distinctive methods of purchase . . . makes them possible."

[30] Brief for Petitioner, p. 5: "This has been the practice as far back as anyone presently with the company can recall."

[31] It is somewhat significant to note that FTC did not apply for certiorari.

[1] 306 F.2d 48 (7th Cir. 1962).

[2] 49 Stat. 1526 (1936), 15 U.S.C. § 13(a) (1958).

Section 2(a) of the act, as amended, provides in part:

It shall be unlawful for any person engaged in commerce, in the course