

## Chapter 3

# Price Discrimination

## Introduction

Two major pieces of federal legislation deal with two aspects of price discrimination:

1. Clayton Act (1914)
2. Robinson-Patman Act (1936).

## Clayton Act

### Statutory Background

The Clayton Act was enacted in 1914 and amended the Sherman Antitrust Act which was earlier enacted in 1890. The Clayton Act was then amended in 1936 by the Robinson-Patman Act and codified at 15 USC §13. The essence of the law is three-pronged:

1. There shall be no discrimination in price or services among individuals, businesses or trusts . .
2. Where restraint of trade is a goal or a result...
3. Unless such price/services differential has an economic justification...
4. With good faith defense being acceptable.

Some eighty years of litigation have to a great extent clarified the meaning of the law's wording. In the section which follows, such case law is briefly summarized for the reader's edification. Because of the volume of the court decisions (well in the hundreds), legal citations are not provided.

### Purpose

The present purpose of the Act was to declare four acts illegal where such acts relate to commodities:

1. **Discrimination**  
The price must be the same when price-sensitive products are sold to similarly-situated buyers.
2. **Tying and Exclusive Dealing Agreements**  
It is illegal to condition the sale of a product on the buyer agreeing to not deal with the seller's competitors..
3. **Corporate Mergers, Acquisitions or Consolidations**  
The effect of such activities must not be anti-competitive.

#### 4. **Interlocking Directorates**

This is where the members of several boards of competing companies are the same person. These arrangements are often dispositive to price discrimination.

These four activities must not result in the lessening of competition. Specifically excluded as affected organizations are the following:

- Labor Unions
- Agricultural cooperatives.

The Act empowered private parties, where they were injured, to sue for treble damages. The Act is enforced by:

- FTC
- DOJ (Antitrust Division).

### **Litigation Background**

The litigation background is summarized as follows:

#### **In General**

Purpose of the law  
Meanings and Interpretation of words  
Sales involving governments  
Relation to other statutory or regulating provisions  
Enforceability of contracts

#### **Meaning of Commerce**

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##### **In General**

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U.S. or foreign market  
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What constitutes a purchase or sale  
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##### **Commodities of Like Grade or Quality**

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Status of particular parties as competitors

##### **Certain Sales Practices Prohibited**

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**Good Faith Defense**

**In General**

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Applicability of provision

Test of good faith

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Effect of unlawful pricing

Effect of duration of price reductions

Enabling buyer to meet competition

**Applicability of Defense to Certain Price Reductions**

Overview

Gaining new clients

Underwriting competitor's prices

**Defenses to Practices Other than Price Reductions**

**Commissions, Brokerage or Other Forms of Competition**

In General

Unconstitutionality

Anti-competitive effect

**In General**

**Purpose of the Law**

The original purpose of this law was to protect the small firms that were unable to purchase in large quantities and had a competitive disadvantage with the large cooperative interstate firms. The miscreants practiced discrimination and not conspiracy. The act was to curb and prohibit all types of price and/or service discrimination caused by a concentration of selling or purchasing power. The main concern of Congress was the dominance of the chain stores which brought on the new danger to fair trade; i.e., buyer concentration of economic power. Congress specifically did not intend to disturb or curtail the disciplines already in place which affect seller competition.

The law does not modify the lawful and normal competition between retailers; nor does it protect the interest of one customer at the expense of another. Congress wanted to obviate price discrimination, to the extent reasonable, which might threaten merchants and businesses, presumably from any source. Congress intended, to the extent practicable, that businesses, at the same functional level, would enjoy reasonably equal competitive terms as regards price and service.

It is important to recognize that essential to the act's purpose, is the pressure of some form of predatory pricing as an act of restraint of trade.

The price discrimination which is the subject of the law may be either direct or indirect. The intended beneficiaries of the law are not the businesses but the general purchasing public.

One of the common features of the law is that its application will nearly always involve a specific commodity; also, a typical characteristic of a violation of the law is the losing of profits (short run) but the gaining of a monopolistic advantage (long run).

### **Meaning and Interpretations of Words**

The act is characterized by words with nebulous and uncertain meaning. As for discrimination, having a rational basis does not remove the taint of *discrimination*. The courts, because of the loose wording of the act, are free to offer their own interpretation and as a consequence, set economic policy. The interpretation offered by the FTC is not determinant but does demand respect.

*Conspiracy* is not a necessary element in the violation of the law. While *chain stores* may be the target of portions of the act, it is by no means limited thereto.

### **Sales Involving Governments**

Where governments act as businesses they should accordingly be treated as such. The law's terms of *person* and *purchasers* are broad enough to include government entities. Where the government entity is acting on its own, the law does not apply; e.g., and army-navy store or PX. Straight-out government supplies purchased from business are exempt.

### **Relation to Other Statutory or Regulating Provisions**

Selling at reasonably low prices solely for the purposes of destroying competition is a criminal act and should be punished accordingly.

The law did not apply to the contract under which an Rx company provided Rx to a hospital where such Rx was for the hospital's use only.

A state had a law that required that a gas supplier must extend all voluntary price reductions uniformly to all service stations. The court had to decide whether this state law was preempted by the federal price discrimination law or would be permitted to stand. The state law was permitted to stand (i.e., not be preempted) for these reasons:

- The limited and localized price discrimination is not so severe as to warrant a preemption of the entire law.

- No federal right to engage in price discrimination is found in the federal right to competition.
- Any conflict between the state law (favoring anti-competition) and the federal laws (favoring competition) is not sufficient to invalidate the state law.

Where the business (bank, e.g.) follows the regulations of the Federal Reserve or the FDIC, it cannot be challenged as being illegal.

The activity of the seller was to inquire as to the prices of its competitors; it did so by calling them and asking their price. This was found to **not** be price discrimination because:

- Purpose of the calls was to comply with, not violate, the law.
- Attempts had been made, unsuccessfully, to obtain the price information.
- The seller had valid reasons to doubt the assertions of the prospective purchaser.
- Only a single buyer and a single price were involved.

It is possible to have price discrimination without any competitive damage but the disfavored purchaser must show damages to it that are part of the anti-competitive effect of price discrimination.

One does not have to wait for price discrimination to become an antitrust issue; its mere existence constitutes a violation.

The price discrimination rule permits a seller from selling at different prices to different buyers but the seller must meet the cost justification rules set forth in the law. Price discrimination exists whether its motives were monopolistic or not. It is a violation of the act to practice price discrimination.

State law required alcohol makers to sell to the state's liquor wholesales at *most-favored nation* terms. The alcohol makers protested claiming price discrimination. The court held that this was not price discrimination.

### **Enforceability of Contracts**

The presence of price discrimination does not invalidate an otherwise valid contract; however a promise to pay a commission, brokerage or other compensation in violation of the law is illegal and does not have to be paid; but it does not invalidate an otherwise valid contract. Violations of antitrust and of contract law must be treated individually. Price discrimination is no defense against a breach of contract claim.

### **Meaning of Commerce**

Where monopolization or restraint of trade must involve interstate commerce, such is also a requirement for price discrimination. Clearly any antitrust infraction must be interstate for it to be a federal matter.

## **Price Discrimination**

### **In General**

Such price discrimination may be either direct or indirect. There are violations of 15 USC §13 (a) other than price differences; e.g., customer selection. The purpose of this law is to see that a purchaser from a single supplier will not be harmed by the supplier's discriminatory practices. Unconsummated sales do not constitute infractions.

The accused price discriminator was able to show that the aggrieved buyer could have obtained the products subject to the price discrimination at the same or lower prices from other markets. The court held this to not be any valid defense against the alleged price discrimination.

There is no price discrimination where two products are commercially equal which occurs when the price differential is consonant with such factors as (a) consumer preference (reflective of advertising and hype), (b) name recognition and (c) quality as well as price

Price discrimination does not apply to leasing transactions. Price discrimination does not have to be repetitive; a sporadic instance of such is an infraction so long as deleterious consequences may be shown. Price, for purposes of discrimination, is gross price less discounts, rebates, offsets and allowances. The law is not concerned with non-price discriminations.

To make a *prima facie* case of price discrimination these essentials are necessary:

- Must be *in commerce*
- The discrimination must be in price as relates to two or more purchases of products of like quality
- Price differences cannot be cost-justified.
- Effect must be to lesson competition.

Price discrimination is bad; price differences are good.

### **Constitutionality**

The language of the law is not so vague as to violate due process.

### **Relation to the Sherman Act**

Geographic price discrimination are infractions of either 15 USC§13 a or 15 USC§13 (a). Mere discounts, rebates and offsets are not *services or facilities* as contemplated by the law.

### **US or Foreign Market**

The law relates to domestic commerce; it does not extend to imports or exports. In this arena, there may be price discrimination of all kinds.

### **Two-Purchase Requirement**

A single sale cannot be an infraction; there must be at least two transactions in order that the law is violated. This is because the law reads *between different purchasers*. The transactions must be separate and distinct. The transaction must be contemporaneous. An offer does not rise to the level of a sale for this two or more rule.

### **Requirement of Contemporaneous Sales**

The two-sales referred to in the previous subsection must have been contemporaneous-but only reasonably so. This could permit a (a) long term contract and (b) a *spot-sale* to be treated as contemporaneous.

### **Purchasers Knowledge of the Prices of other**

The purchaser is not required to know the details of the supplier's price to others.

### **What Constitutes a Purchase or Sale**

There are arrangements where price is set based upon the quality of service provided by the buyer to its customers. This activity is not price discrimination. Price discrimination is not an illegal activity when done among controlled employers; i.e., intra-corporate sales/transfer are not activities which are controlled by antitrust law; nor are exchanges of *fungible* products or goods. To be a sale for price discrimination purposes, there must be a clear transfer of title.

Price discrimination can apply to lease transactions. What is a division or a separate corporation is a facts and circumstances issue.

The sale for price discrimination purposes occurs when the *deal is struck* and not when the *paper/work is done* and the price paid. Potential buyers have no standing to complain. Also the sale for price discrimination purposes must be *arms-length*.

Settlement prices have no standing where price discrimination is an issue.

### **Who are Purchasers**

Purchasers may include government entities; sales representative who bought as a temporary convenience (and paid by commission) were not purchases even though they could sell to the ultimate consumer with a discount.

## **Anti-Competitive Effect**

### **In General**

The law forbids price discrimination which may be substantially to lesson competition. Mere possibility of specified consequences is not enough; there must be a probable lessening of competition. Factors in price competition might include name/brand recognition.

The distinction must always be made between these two:

1. Price Competition
2. Price discrimination.

### **Price Competition**

This is acceptable even if the effect is to lesson competition

### **Price Discrimination**

This is unacceptable where like goods are sold or bought at different prices unless such is cost-justified.

To have a price discrimination which is an antitrust infraction, there must be reasonable possibility of a restraint of trade; it does not require that any harm actually occurred. The possible evil need not have been seen.

Price discrimination is illegal only if it lowers the price and prevents (or tends to prevent) competition from denying to the merchant (who sets the lower prices) business rewards which its competition might have obtained had merchant not lowered its price below what it was charging elsewhere.

## **Robinson-Patman Act**

### **Introduction**

The Clayton Act amended the Sherman Act by forbidding price discrimination in commodities unless there was (a) cost justification and (b) absence of trade restraint and (c) absence of a rule of reason rationale. This Act dealt with powerful sellers. The Robinson-Patman Act did in effect the same thing except it related to buyers. The Act has been criticized fro being vague and difficult to administer. Only the FTC will typically use it as in regulatory tool.

This Act was passed in 1936 during the deep depression following the emergence of large and very successful food chains. The small family-owned grocery stores lobbied Congress for legislative relief. The actual draft of the Act was provided by the U.S Wholesale Grocers Association.

## **Purpose of the Act**

The Robinson-Patman Act was intended to correct several flaws in the Clayton Act:

1. The Clayton Act was not specific regarding commodities or services.
2. The courts held that the Clayton act did not apply to price discrimination which was based solely on volume; this defect was precisely what the act was to courts.

The Act forbids quantity-based discounts except in certain situations. The Act applies to:

- Sellers who offer discriminatory prices
- Buyers who knowingly receive them.
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For such infractions a private party and FTC may obtain treble damages.

## **Definition of an Infraction**

These jurisdictional elements must be present:

- Commerce (interstate)
- Sales or purchases
- Commodities (including tangibles)
- Like kind and quality.

Multiple sales are essential; price is net of discounts.

## **Typical Defenses offered**

The typical defense will take any/all of the following:

- **Meeting Competition**  
Such low prices were demonstrably necessary to meet the market place prices. If this is shown, the defense is absolute-regardless of competition or competitors.
- **Cost Justifications**  
The actual cost of manufacture, sale, or delivery economically justifies the difference.
- **Functional Availability**  
The defendants need only show that the alleged discount was available to such defendants but for whatever reason was not taken.

The clout and importance of the Robinson-Patman Act have waned in the last few decades for these reasons:

- It is vague, convoluted and obscure.
- The Act is in some ways possibly anti-competitive.
- Public's attitude toward the large chain stores has changed.

## Regulatory and Statutory Issues

The principal decided issues were these:

- *Most-favored nation* state laws do not affect interstate commerce nor are they price-discriminatory.
- So long as other laws or regulations do *not change the flavor* of the antitrust laws; are not in conflict therewith; are not applicable thereto, they are not preempted.
- While the Robinson-Patman Act does not require the commerce to be interstate, for a price-fixing activity to rise to the level of an antitrust infraction, such commerce must be interstate.
- Establishing a predatory price infraction, the issues are the same for either Sherman or Robinson-Patman.
- Robinson-Patman is to stop incipient antitrust infractions.
- Price discrimination under Robinson-Patman becomes a serious matter only when there is also (a) an antitrust infraction or (b) monetary damages.
- If a price discrimination dispute fails to so qualify as a Robinson-Patman infraction, it necessarily fails to be an antitrust infraction..
- Sherman infraction is criminal; Robinson-Patman is civil.