Market Structure, Competition and Regulation in the Distribution of Fluid Milk

Prepared by
A Committee on Milk Marketing
Appointed by
Governor Nelson A. Rockefeller

April 1964
LETTER OF TRANSMITTAL

To the Governor and the Legislature of the State of New York:

We are pleased to transmit herewith a report entitled "Market Structure, Competition and Regulation in the Distribution of Fluid Milk." This report was prepared by a committee appointed by the Governor in April 1961.

Respectfully submitted,

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April 1964
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Governor Rockefeller appointed an eight-member Committee on Milk Marketing in 1961. Among other things, the Committee was asked to consider the question, "Is the distribution system for milk and milk products functioning efficiently and in the best interests of both producers and consumers?"

In April of that year the Governor disapproved a bill commonly referred to as the Drumm-Gordon Bill which would have given the Department of Agriculture and Markets broad authority to fix minimum retail and wholesale prices of milk and to regulate trade practices in the distribution of milk. In disapproving the bill, the Governor urged that the Committee give attention to this problem.

Following is the Committee's statement on this subject. It was developed after a study of the nature of the competitive problems in the industry, the earlier price control experience in New York, and the experiences of other states which have legislated on these matters. The Committee had the benefit of conferences with representatives of producer and distributor groups in the industry, with officials of the Department of Agriculture and Markets and with other knowledgeable persons. The statement, however, is the sole responsibility of the members of the Committee. It does not necessarily reflect the opinions of persons with whom the Committee conferred, nor is it to be construed as representing the views or policies of the institutions with which members of the Committee are associated.
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MARKET STRUCTURE, COMPETITION AND REGULATION
IN THE
DISTRIBUTION OF FLUID MILK

Part I
Market Structure and Competition

Governments, both federal and state, are deeply involved in regulating the dairy industry. New York State, unlike some others, presently has no regulation of retail or wholesale prices of milk. Moreover, the State has relatively little regulatory control over trade practices in the distribution and sale of fluid milk. Many members of the industry contend that the industry is plagued with unfair and destructive trade practices to such an extent that it has become a matter of public concern. Consequently, they believe the need exists for additional regulation to curb competitive abuses.

To assess the need for additional regulation, it is important to have an understanding of the industry's market structure, the changes taking place in the processing and distribution of milk and the competitive situation in the industry. It also is important to know the extent of destructive competition and the impacts of destructive practices upon producers and consumers as well as upon milk dealers and their employees. These matters are considered in this part of the report.

The Marketing System

Distribution Channels

The task of providing consumers with fluid milk in the various forms, quantities and packages desired involves a series of marketing services which are performed by a number of agencies. The major services involved in the marketing of fluid milk include procurement of raw milk from farms, transportation from farms to plants, processing and packaging, advertising, selling and delivery to homes, selling and delivery to wholesale outlets such as food stores, restaurants and schools and retailing by stores or through vending machines.

The two major methods of distributing milk to consumers are delivery to homes and sale through retail food stores. The home delivery system has been a somewhat unique characteristic of the fluid milk industry. Until recently, home delivery was the principal method of distribution in New York State outside the New York City market. Home delivery still accounts for approximately 40
percent or more of the total volume of milk sold in upstate areas. In the New York Metropolitan Area, a much larger proportion of the milk for household consumption is distributed through stores.\footnote{In 1955, approximately 70 percent of the milk sold for household consumption in the New York City market was distributed through stores. Market Administrator's Bulletin, New York Metropolitan Milk Marketing Area, Vol. 15, No. 4, April 1955.}

For reasons discussed later in this report, milk distribution through retail food stores, especially supermarkets, has been increasing and home delivery has been declining during the past two decades. The shift from home delivery to the store distribution of milk has progressed further in large cities than in smaller markets.

In some markets, specialized dairy stores have become increasingly important outlets for milk during the last decade. Some such stores, especially those organized in chains, have been leaders in offering milk at reduced cash-carry prices, usually in half-gallon and gallon glass bottles.

Hotels and restaurants are important outlets for milk, especially in large markets.

Schools have become significant distribution outlets for milk, largely because of the National School Lunch and Special Milk Programs which subsidize milk distribution in schools. Nationally, the quantity of fluid milk (and cream) distributed under these two programs in 1962-63 represented approximately 5.3 percent of total civilian milk consumption.\footnote{Stewart Johnson, Dairy Marketing, Connecticut Agricultural Extension Service, November 1963, page 2.} This was about 11 percent of total milk consumption during the days that schools were in session. In addition to schools, other institutions such as hospitals and military establishments are taking more milk than formerly. Much of the milk supplied to these institutions as well as to schools is sold under contracts that involve public bidding.

Vending machines of both indoor and outdoor types are being used to a greater extent than formerly for the sale of milk. As yet, however, this outlet probably accounts for no more than one or two percent of the milk distributed in most markets.

Specific information on the importance of different sales outlets for milk is available for the Niagara Frontier and Rochester markets (Table 1). By 1962, more than one-half of the milk purchased for home consumption in these two markets was being distributed through stores. Schools in the Niagara Frontier and Rochester markets have become more important trade outlets for milk, as they have nationally. The sale of milk to institutions which include hospitals, nursing homes and the like has not changed markedly in the Rochester and Niagara Frontier markets during the periods reported. There are no large military installations in either of these two markets.
Table 1. Relative importance of various trade outlets for whole milk, Rochester and Niagara Frontier markets, New York

<table>
<thead>
<tr>
<th></th>
<th>Rochester, New York</th>
<th>Niagara Frontier</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>May 1944</td>
<td>May 1954</td>
</tr>
<tr>
<td>Home delivery</td>
<td>61</td>
<td>54</td>
</tr>
<tr>
<td>Wholesale:</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Stores</td>
<td>21</td>
<td>30</td>
</tr>
<tr>
<td>Restaurants</td>
<td>13</td>
<td>10</td>
</tr>
<tr>
<td>Institutions*</td>
<td>3</td>
<td>3</td>
</tr>
<tr>
<td>Schools</td>
<td>2</td>
<td>3</td>
</tr>
<tr>
<td>Total wholesale</td>
<td>39</td>
<td>46</td>
</tr>
<tr>
<td>All outlets</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

* Includes sales made to hospitals, orphanages, nursing homes and the like.


Marketing Agencies

Traditionally, most of the services involved in marketing fluid milk, other than store retailing, have been performed by milk dealers. Many milk dealers have performed or controlled a whole series of marketing services including procurement, country handling, transportation, processing and packaging, depot and delivery operations.

In recent years, however, certain non-integrated or specialized marketing agencies have become important in the marketing of milk, especially in large metropolitan markets. Many country plants are operated by farmer cooperatives or proprietary firms that do not operate pasteurizing plants or other facilities. At the other end of the system, increasing volumes of milk are being distributed by firms that buy bottled or packaged milk from a processor, commonly known as subdealers or agent distributors.

Within the last few years certain large dealers have contributed to the development of subdealers. For example, the Borden Company and National Dairy Products Corporation have disposed of their retail delivery routes in New York.
City and certain other metropolitan markets. The disposal of these routes has been made in some instances under contract to branch managers or drivers who continue to distribute the companies’ products.

As explained previously, increasing volumes of milk are being sold through stores, usually operated independently of milk handlers. In addition, a few dealers specialize in supplying vending machines.

Although non-integrated or specialized marketing agencies are increasing in importance, some significant steps toward more vertical integration in the industry also are evident. In a number of instances, cooperative associations of milk producers, whose main function is bargaining, have undertaken certain phases of the physical marketing of milk. Many cooperatives operate country receiving plants, and some operate milk manufacturing plants. A few operate pasteurizing and packaging plants and distribution systems. The Dairymen’s League Cooperative Association, Inc., and certain cooperatives in the Niagara Frontier and Rochester markets perform all marketing functions, and also represent producers in marketing order matters, negotiations with handlers, and in other ways.

Another form of vertical integration involves the entry of certain supermarket chains into the operation of milk pasteurizing plants and delivery systems. So far there has been relatively little of this in New York State, though at least three food chains in the State take delivery of milk at the processors’ plants (i.e., First National Stores, Inc., P & C Food Markets, Inc., and Victory Markets, Inc.). Examples of chain store integration in other areas include Stop and Shop, Inc., in New England and Safeway Stores, Inc., and the Kroger Company, which operate their own milk pasteurizing plants in certain other parts of the country.

Specialized dairy stores constitute another form of vertical integration that has become increasingly important in recent years. With this method of distribution, the procurement, processing, packaging and transportation of milk and the operation of stores are performed by the same firm. Recent examples of this development in New York include the Dairy Barns, Cherry Valley Stores and Old Dutch Farms on Long Island; Perkey Milk Company in Eastern New York; Farmer-In-The-Dell in the Capital City area of New York; and Briggs and Kauderer’s Dairies in Western New York. Lawson’s Dairy in Ohio and High’s Dairy in the Washington, D. C. area were among the early developers of this type of operation. More recently Cumberland Farms, Inc. has expanded its dairy store operations rapidly in New England and in New Jersey. Certain milk dealers in New York State markets operate one or more dairy stores or milk depots, frequently in conjunction with their plants.

Number and size of dealers. The usual situation in most markets is that nearly one-half or perhaps more than one-half of the business is done by two, three or four major distributors. The remainder commonly is done by many smaller firms (Table 2). It is not unusual for the largest distributor in a market to have 30 percent or more of the total sales.
Table 2. Average and range in the number of pool handlers and the
percentage of sales accounted for by the four largest handlers in
71 federal order markets, United States, March 1962.

<table>
<thead>
<tr>
<th>Total sales of pack-aged fluid milk by pool handlers located in</th>
<th>Number of milk handlers</th>
<th>Percent of total sales handled by four largest handlers</th>
</tr>
</thead>
<tbody>
<tr>
<td>same counties as four largest pool handlers (million pounds)</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Number of markets</td>
<td>Total in any market</td>
</tr>
<tr>
<td>Less than 8.0</td>
<td>17</td>
<td>154</td>
</tr>
<tr>
<td>8.0 - 15.9</td>
<td>24</td>
<td>382</td>
</tr>
<tr>
<td>16.0 - 23.9</td>
<td>10</td>
<td>202</td>
</tr>
<tr>
<td>24.0 - 59.9</td>
<td>15</td>
<td>423</td>
</tr>
<tr>
<td>60.0 or more</td>
<td>5</td>
<td>338</td>
</tr>
<tr>
<td>All markets</td>
<td>71</td>
<td>1,499</td>
</tr>
</tbody>
</table>

Source: Alden C. Manchester, Marketing Economics Division, Economic Research Service, United States Department of Agriculture.

In Rochester, New York, a market with average monthly fluid milk sales of approximately 14 million pounds, the four largest firms processed about 65 percent of all the fluid milk packaged in the market in October 1962. As in most markets, the distribution and sales operations were not as concentrated as the processing operations. In Rochester the four largest dealers distributed approximately 48 percent of the milk in the market in October 1962 (Table 3.). Seventy-four other distributors had the remainder of the business. In the Niagara Frontier market, with monthly sales averaging about 30 million pounds in 1962, the four largest firms distributed approximately 39 percent of the milk in the market in October 1962 (Table 3.). The remainder of the business was shared by 105 other distributors.

It appears that the concentration of processing in the hands of the four largest firms in the New York City and the Nassau, Suffolk and Westchester counties area is approximately the same as the average for the five largest federal order markets reported in table 2. The four largest firms in the New York City area probably control less of the distribution than of the processing, even though some processors may exhibit some control over the competitive practices of the distributors for which they process.

1/ Market Administrator, the Rochester Milk Marketing Area, Department of Agriculture and Markets, State of New York.
Table 3. Number and size of milk dealers in Rochester and Niagara Frontier markets, New York, October 1962.

<table>
<thead>
<tr>
<th>Average number of quarts sold per day</th>
<th>Rochester</th>
<th>Niagara Frontier</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Number of dealers</td>
<td>Percent of total units sold</td>
</tr>
<tr>
<td>Less than 484</td>
<td>23</td>
<td>2.1</td>
</tr>
<tr>
<td>484 - 968</td>
<td>20</td>
<td>5.0</td>
</tr>
<tr>
<td>969 - 1,613</td>
<td>6</td>
<td>2.5</td>
</tr>
<tr>
<td>1,614 - 3,226</td>
<td>17</td>
<td>12.6</td>
</tr>
<tr>
<td>3,227 - 19,354</td>
<td>8</td>
<td>29.6</td>
</tr>
<tr>
<td>19,355 or more</td>
<td>4</td>
<td>48.2</td>
</tr>
<tr>
<td>Total</td>
<td>78</td>
<td>100.0</td>
</tr>
</tbody>
</table>


Note: The number of dealers reported in table 3 is not directly comparable to the number of handlers cited in table 2. The data in table 3 include some distributors (e.g., subdealers and perhaps some out-of-market handlers) who would not be classified as handlers under a marketing order. The figure cited in the text, page 5, indicating that the largest four firms processed about 65 percent of the milk in the Rochester market is more directly comparable to the concentration data in table 2.

There has been a definite trend in most markets toward a decrease in the number of milk dealers, especially among the smaller firms. In Rochester the total number decreased from 120 in 1944 to 78 in 1962, with the number of dealers selling less than 3,227 quarts a day decreasing from 111 to 66 and the number selling 3,227 quarts or more a day increasing from nine to 12.

A recent study by the U.S. Department of Agriculture indicates that the decrease in number of milk distributors has not necessarily resulted in an increase in the proportion of business in the hands of the largest four handlers. In some markets, the business has become more concentrated; but in others, less concentration has resulted.


As the milk marketing system has developed in the United States, especially since about 1925, there has been a strong trend toward expansion of marketing firms both by internal growth and by means of mergers or consolidations. The process of merger and consolidation of plants and dealers has reached the point where there are now several dairy companies of large size. Six companies (i.e., National Dairy Products Corporation, Borden Co., Beatrice Foods Co., Foremost Dairies, Inc., Carnation Co., and Arden Farms, Inc.) each had total sales in 1962 exceeding $400 million. The two largest dairy firms, National Dairy Products Corporation and the Borden Company, operate fluid milk businesses in New York State.

Trade associations. Milk dealers in the State are organized in various trade associations. Those in each of the major markets have a local association. These local associations in upstate markets, in turn, are members of the New York State Milk Distributors, Inc. In addition, many distributors in small markets where there are no local associations are direct members of the State association. The membership includes some cooperatives as well as proprietary dealers.


Most of these trade associations perform a number of services for their members, although some are quite specialized. All of them perform public relations tasks for their members. Some represent dealers in labor contract negotiations, legislative matters, marketing order hearings, contacts with health department officials and the like. In addition some trade associations assist their members by providing market and credit information, insurance plans and product promotion materials.\(^1\)

Unions. A large proportion of the employees of the dairy industry in New York are members of labor unions. These include plant workers, deliverymen, and over-the-road transport drivers. Most are members of the Teamsters Union but some are represented by other unions. Serious labor disputes and occasional work stoppages have occurred in connection with the negotiation of labor contracts, particularly in the New York Metropolitan Area. Unions have taken an active interest in trade practices. Some labor contract provisions (e.g., provisions calling for relatively high commission rates for wholesale deliverymen, those restricting the adding of new products to a route and those restricting the sale of milk at the plant platform) directly affect trade practices and in some instances, limit the ability of dealers to adjust to changing conditions.

\(^1\) F. D. Mills, Milk Dealers’ Trade Associations With Special Reference to New York State, M.S. Thesis, Cornell University, Ithaca, New York.
Major Changes in Processing and Distribution

Significant changes are taking place in the processing and distribution of fluid milk. The rate of change in the industry has been much more rapid during the last decade than in previous years. The rapid pace of technological changes and innovations in the transportation, processing, packaging, and distribution of milk has had a tendency to disrupt established marketing arrangements and price structures. Developments such as these have created serious problems of adjustment for many milk dealers, cooperatives, and employees, and have stimulated distributors' demands for regulation of resale prices and trade practices.

Changes in Processing

The fluid milk processing industry is undergoing some rapid changes, caused primarily by the adoption of new technology aimed in large measure at saving labor. Plant operators have attempted to reduce costs by substituting capital for labor as labor rates have continued to rise faster than the cost of labor-saving equipment.

The major structural change in fluid processing is the trend toward fewer and larger plants. The number of pasteurizing and bottling plants has decreased significantly in the last two decades even though there has been a significant increase in the total quantity of milk processed. Similar changes have occurred throughout the country.

A major reason for the trend toward fewer and larger plants is the increased advantage of large-volume plant operations under present-day conditions. Many factors affect the costs of operating pasteurizing and packaging plants, but the most important single factor affecting the cost per unit is the quantity of milk handled in the plant. Larger plants generally are able to achieve lower unit costs than smaller plants because they are able to obtain higher output per hour of labor and per dollar of investment (Table 4).

These and other data\(^1\) indicate that the costs per quart of processing and packaging milk decrease sharply as the size of the plant increases, especially up to a daily output of 20,000 quarts. Beyond that point unit costs decrease at a slower rate as plant volume rises.

Specific investment and cost data are not available for plants that process quantities of milk in excess of 100,000 quarts a day, although there are several such plants in the New York Metropolitan Area.

\(^1\) M. C. Conner, F. C. Webster, and T. R. Owens, An Economic Analysis of Model Plants for Pasteurizing and Bottling Milk, Virginia Agricultural Experiment Station Bulletin 484, June 1957.
Table 4. Relation of plant size to capital requirements and cost per unit in fluid processing plants*

<table>
<thead>
<tr>
<th>Capacity of plant (quarts daily)</th>
<th>Investment per quart of daily capacity</th>
<th>Total costs per quart+</th>
</tr>
</thead>
<tbody>
<tr>
<td>6,000</td>
<td>$24</td>
<td>$.057</td>
</tr>
<tr>
<td>20,000</td>
<td>11</td>
<td>.039</td>
</tr>
<tr>
<td>50,000</td>
<td>8</td>
<td>.032</td>
</tr>
<tr>
<td>100,000</td>
<td>7</td>
<td>.029</td>
</tr>
</tbody>
</table>

* These data were developed using model plant or budgetary analysis. They represent, therefore, well-managed operations with a high degree of efficiency. The plants were planned to process a rather wide range of products in a number of types and sizes of containers. They were specified to handle both paper and glass containers.

+ Reflects all plant costs, including containers. Approximately 50 percent of the total volume in each plant was packaged in paper containers.

Source: F. C. Webster, Alec Bradfield, J. R. Bowring, K. A. Taylor, and H. C. Moore, Economics of Size in Fluid Milk Processing Plants, Vermont Agricultural Experiment Station Bulletin No. 636, June 1963, pages 5 and 8.

Improvements in dairy plant equipment have occurred more rapidly during the past decade than previously. Rising labor rates have stimulated efforts of plant operators to save labor by installing labor-saving equipment. The added investment in equipment has been reflected in higher fixed costs, thus increasing the advantage of large-volume operations.

The increased advantage of larger-scale plant operations, together with improved transportation facilities, the use of paper containers in place of glass bottles and the availability of large-volume sales outlets, such as supermarkets, have made it economically feasible to distribute milk over greater distances from a central plant. These developments have been the principal factors leading to the elimination of many small pasteurizing plants.

Despite many plant consolidations during recent years, a large number of plants of smaller than optimum size still are being operated, especially in upstate New York. Operators of some of these small plants are able to offset their relatively high processing costs through locational advantage or by working long hours and accepting relatively low returns on their investments. In view of the economies of size in plant operations, and the changes taking place in distribution, however, it is apparent that many plant operators are working under a serious handicap. Consequently, plant consolidations are likely to continue. The
extent and rate of these consolidations will depend in part on how rapidly labor rates increase and upon the degree of price competition that prevails.

Another important factor affecting processing costs is the number and types of products and the kinds and sizes of containers used. In recent years, many milk plant operators have reduced the variety of products that they process, but even so most plants still process several products and package them in different types and sizes of containers. In some instances, however, plant operators have achieved high labor efficiency with only modest volumes of milk by confining their operations to a limited line of products and packages. The trend to greater specialization of plant operations is likely to continue as competitive pressures force milk dealers to reduce costs.

Changes in Distribution

Shift away from home delivery. As previously stated, until recently home delivery was the most important method of distributing fluid milk in most markets of the United States. This method involves more service than others and, therefore, tends to be a relatively high-cost form of distribution. Although home delivery continues to be an important method of distribution, the shift from home delivery to store distribution is one of the major adjustments taking place in the industry. Home delivery operations are particularly important to many relatively small distributors, who can compete successfully with large firms for home delivery business but who are at a severe disadvantage in competing with large, multi-product, geographically diversified firms, for the milk business of large food stores.

A major reason for the shift away from home delivery has been the increasing difference in price between home-delivered and store milk in many markets. This widening differential, in turn, has been due largely to rising labor rates and to the fact that the output per hour of labor is much higher on wholesale routes than on home delivery routes. A given increase in wages and fringe benefits for routemen generally raises the cost per quart on home delivery routes two to five times as much as it does the costs of distribution to stores. Furthermore, the size of loads on routes serving stores generally has increased in recent years while the size of loads on most home delivery routes has remained about the same since the every-other-day delivery system was adopted during World War II.

Other factors no doubt have contributed to the trend toward the increasing importance of stores in the distribution of milk with the corresponding decline of home delivery. Among these factors are the following: the increased size and importance of urban areas; the improved keeping quality of milk; improved refrigeration in delivery, at stores and in homes; the use of good lightweight paper containers; certain changes in family living and working habits; and the aggressive merchandising of milk by the operators of many supermarkets and dairy stores.
Increasing importance of large food stores. The shift from home delivery to the store distribution of milk has occurred during a period in which the number and importance of large food stores have increased sharply. In 1952 about five percent of the grocery stores in the country had annual sales of more than $500,000 a year, and these stores had about 39 percent of total grocery store sales. Ten years later, about 11 percent of the stores were of this size, and they had about 68 percent of the total sales. The sharp drop in the number and importance of small food stores and the rapid growth of supermarkets have had an important effect on milk distribution and the competitive structure of fluid milk markets.

Large differences in costs of serving stores. Delivery costs per quart vary widely with the quantity of milk and other dairy products delivered to a store. The findings of a recent study in New Jersey illustrate the relationship between the quantity of products delivered to a store and the delivery cost per quart (Figure 1).

This study indicates that the delivery cost per quart decreases sharply with increases in the quantity of products delivered, up to approximately 100 units per delivery. Delivery costs per quart continue to decrease with still larger deliveries, but at a slower rate. A supermarket taking 360 or more quarts per delivery can be served at a very low cost per quart as compared to stores receiving 50 quarts or less per delivery. This volume-cost relationship indicates a principal reason why stores handling large quantities of milk commonly are able to buy milk at lower prices than smaller stores. This is usually accomplished through discounts or by other concessions granted by the supplier.

In most markets, a large proportion of the food stores sell rather small quantities of milk per day while relatively few, very large stores sell large quantities. A survey of 264 food stores in Manhattan, Brooklyn, Bronx and Queens in 1957 indicated that the 100 smallest stores, or 38 percent of the total, sold an average of less than 117 quarts of fluid whole milk, skim milk and butter-milk a day. These 100 smallest stores, about half of which sold more than one brand of milk, sold less than 11 percent of the milk sold by all the stores surveyed. On the other hand, the 74 largest stores surveyed, or 28 percent of the total, sold 318 or more quarts a day and accounted for 67 percent of the milk sold by all stores in the study.

In five upstate New York markets (i.e., Syracuse, Buffalo, Utica, Rochester and Albany), small stores representing 34 percent of 272 stores surveyed sold less than 50 quarts a day. They accounted for only seven percent of the total milk sales made by the stores surveyed in this 1957 study. Stores selling 318

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1/ Economic Inquiry into Food Marketing, Staff Report to the Federal Trade Commission, January 1960, page 53.
or more quarts a day and representing only six percent of all stores surveyed sold approximately 30 percent of the milk.

Thus, in most markets there are a relatively large number of small-volume stores that can be served only at relatively high cost per unit and a relatively small number of large-volume stores that can be served at much lower unit costs. Moreover, many of these larger stores are members of chain organizations or voluntary buying associations which further strengthens their bargaining position as buyers of milk.

Several factors affect the relationship between the quantity of products delivered to a store and the delivery cost per quart. These include the level of fixed cost per route, the commission rates paid the routeman and the amount of service provided. The higher the base pay and the lower the commission rate, the greater the cost saving per quart in serving stores that take large quantities
of milk. Generally, pay plans in the New York Metropolitan Area provide for higher base pay and lower commissions than wage agreements in the upstate markets. Consequently, the difference in the unit costs of serving stores that take small quantities and those taking large quantities tends to be greater in the New York Metropolitan Market than in many upstate markets.

Generally the more service provided by the routeman to the store, the larger the difference in the unit cost of serving stores taking various quantities of milk. The data in figure 1 reflect the costs incurred by relatively efficient dealers on routes where the deliverymen provide most stores with typical amounts of service (i.e., the routeman obtains order, places products in the cooler and obtains receipt of delivery). They do not reflect economies that can be achieved through limited service delivery to stores. Some stores receive only drop delivery (i.e., the routeman merely unloads the milk and does not move it into the store’s cooler). According to the New Jersey study, providing drop delivery instead of inside delivery to stores taking 19 cases of product resulted in an average saving of about one-half cent a quart.1/

The keen competition among stores is likely to encourage large supermarkets to continue to insist that the prices they pay for milk reflect the relatively low unit costs at which they can be served. As discussed later, most supermarket operators are concerned about being fully competitive with other stores in the sale of milk. Moreover, many supermarkets are in a strong position in bargaining with milk dealers. Since a large proportion of the total cost of operating a delivery route, as well as many of the costs of processing, are fixed, the loss of a large supermarket customer would decrease the dealer’s income appreciably without a comparable reduction in his costs. Or, to put it another way, an additional large store can be served at relatively small extra cost if the plant and route involved are not operating at full capacity. The bargaining position of some supermarkets is strengthened by the fact that they have alternative ways of procuring milk and other dairy products.

Specialized delivery systems to serve supermarkets. In some markets, specialized milk delivery operations have been established to serve groups of large supermarkets. In certain cases, these specialized routes are operated by milk dealers (e.g., Borden Company’s routes serving A & P food stores in the New York Metropolitan Area, and Crowley’s Milk Company’s routes serving Loblaw food stores in South Central New York). But as noted earlier some food store chains operate their own delivery routes. In other areas, some food chains also have undertaken the operation of their own fluid milk processing plants as well as delivery routes (e.g., Stop and Shop, Inc., in New England, and the Safeway and Kroger Companies in other areas).

Increasing importance of specialized dairy stores. Another significant development in milk distribution has been the increasing number and importance of specialized dairy stores. Dairy stores frequently have been opened in areas where the operators had little or no distribution previously. In other cases, small or medium-sized independent distributors are opening dairy stores because they are losing their home delivery businesses to supermarkets and cannot compete successfully with large dealers for supermarket business.

Most dairy stores emphasize the sale of milk, fluid milk products, ice cream and cottage cheese. In addition, however, they usually carry other dairy products and some non-dairy items such as bread, cookies, soft drinks and cigarettes. Milk usually constitutes a large percentage of a dairy store's total sales. These stores usually are operated on a self-service basis and often are manned by a single clerk except at peak hours. Many dairy stores employ non-union labor, operate on a seven-day-a-week basis, and are open long hours each day.

In terms of customer service and distribution costs, dairy stores represent the opposite extreme from home delivery. Dairy stores provide less service than other methods of distribution and, in most instances, are low-cost operations. The customer who buys at a dairy store serves herself, pays cash, pays a deposit on the bottle, and performs her own delivery service. Consequently, this method of distribution involves a minimum of labor expense and container cost and avoids credit costs.

Specialized distribution systems have resulted in reduced retail milk prices and distribution margins in many markets, and have accelerated the decline of home delivery. The primary basis for their pricing policies appears to be the low costs that can be achieved with these limited service types of distribution systems. The supermarket chain that processes and delivers its own milk and the specialized dairy store operator can couple efficient, specialized plant operations with low-cost distribution. Milk can be moved from the processing plant to the supermarket or dairy store at exceptionally low costs because of savings from limited service and the large quantities of product delivered per store. These systems also benefit from the flexibility they permit in organizing the time and frequency of delivery and more economical labor arrangements (i.e., non-commission wages for deliverymen and longer working hours in many cases).

These specialized distribution systems serve only a minor portion of most markets because the majority of consumers prefer and are willing to pay for additional service. Even so, firms conducting such specialized operations can acquire a sufficient volume of sales in many markets to permit the development of efficient and profitable businesses and at the same time provide many consumers with a combination of product, service and price they prefer over other

1/ See New Jersey study, op. cit., exhibit 7.
alternatives. In some instances these systems have had the benefit of institutional arrangements not available to other dealers. For example, in many cases, the specialized operators employ non-union help and pay straight wages with no commission to deliverymen.

Increasing importance of institutional outlets. Institutional outlets such as schools, public institutions and military installations, have become increasingly important outlets for milk. Milk distributors are given the opportunity periodically to submit bids for these outlets. Such contract sales can add importantly to a distributor's volume and thus enable him to operate closer to capacity. One or more dealers are usually in a position to handle the additional volume involved in such a contract with comparatively little extra cost. Consequently, the bidding for such contracts has become a significant element in the competition among distributors. However, this is not the type of competition about which most dealers complain.

Increased importance of vending machines. In some markets increasing quantities of milk have been sold through vending machines in recent years. Machines for on-premise consumption are located in industrial plants, office buildings, department stores, schools, terminals, and similar places. In addition, increasing quantities of milk for home consumption have been sold through vending machines. These machines are located in large apartment houses as well as in convenient outdoor locations. Vending machines make milk available to consumers at times and places more convenient than other outlets provide. Vending machines are reported to have been used by some distributors as a competitive device to enter a new market area and by others as a means of regaining lost business.

Adjustment Problems Faced by Distributors

Such important changes in cost relationships, distribution methods and market structure pose difficult problems for many processors and distributors, as well as their employees. Many small and medium-sized distributors who have been able to compete successfully with large dealers in home delivery operations in the past find they are too small to compete successfully for the milk business of large food stores, especially chains.

Some large distributors also face major problems in making needed adjustments. In many instances, labor contracts and arrangements pose important barriers to adjustment. As stated, new operators frequently have an advantage because of their ability to hire non-union help or at least to start with more favorable labor arrangements. Well-established large distributors, who would appear to be in the best position to make adjustments, face problems because it is difficult for them to make special delivery arrangements for certain customers such as large supermarkets without disrupting their relationship with others. Established distributors have a legacy of their past operations. They are disadvantaged in adopting new methods as compared with new operators with no existing commitments.
Competition Among Milk Dealers

Milk dealers, like most other businessmen, compete with one another in the pricing of their products as well as in services offered and in the variety, quality and packaging of products sold. They also compete through advertising, solicitation and the like. In general, however, milk dealers have tried to avoid outright price competition.

Prior to the late 1940’s, when home delivery was dominant and price discipline among dealers strong, there was considerable stability and uniformity in retail milk prices in most markets. In recent years, however, price stability and uniformity have been disrupted frequently. The increased tendency towards price competition and the greater variability in milk prices have disturbed many members of the industry, and they have sought legislative remedies.

Interdependence of dealers in pricing. Several basic competitive conditions exist in most fluid milk markets that tend to cause a high degree of interdependence in pricing policies among milk dealers. These conditions include: 1) the relatively small number of firms of appreciable size in most markets, 2) the high substitutability of brands of milk, 3) the fact that total consumption in a market changes less proportionately than price, and 4) the fact that dealers' buying prices for raw milk are largely fixed by federal or state marketing orders in all of the principal markets in the State.

Under these conditions, most established milk dealers recognize the probability that price reductions will be met by competitors and that a reduction in the market price will reduce total sales revenues to distributors. Only a distributor with a small proportion of the business of a market can expect that his price reductions will not be matched by competitors. Furthermore, most milk distributors are aware of the danger of retaliatory price reductions. Although milk distributors recognize that a market-wide increase in price would increase total revenues, any one distributor is reluctant to raise his prices because of fears that his competitors will not follow. Enlightened, established dealers, therefore, normally practice a considerable amount of self-restraint in their pricing for fear of uncooperative or retaliatory action by their competitors. There is a strong tendency to follow a “live and let live” policy in pricing. Such a tendency is observed in many other parts of the American economy.

Over the years, price leadership, the pattern of following the prices of some identified leader(s), has existed in milk markets in New York State, as well as in other areas. As mentioned previously, retail prices have had a strong tendency to be uniform within markets and stable over rather long periods of time. Until recently price changes tended to occur infrequently, usually when labor rates or raw milk costs changed.1/
In the competitive environment that prevails in the milk distribution industry, the step from a high degree of self-discipline among competitors to price fixing through collusive agreement is small. It is difficult to distinguish between actions that result from collusive agreement among competitors and those that reflect price leadership.

While this Committee is seeking primarily to determine whether there are abuses which take the form of destructive competition, it cannot ignore occasional evidences of inadequate competition among dealers. Hence, it is concerned with reports of the filing of identical price schedules by several dealers in bidding on contracts for supplying milk to schools, including instances in which more than one-half dozen different products and packages were priced exactly the same. Likewise, the Committee is concerned with reports of instances where dealers have threatened to discontinue service to a food store unless the latter agreed to sell at prices no less than those stipulated by the dealers.

The ability of dealers in many markets to avoid outright price competition through market-wide discipline has shown an increasing tendency to break down in recent years. The reasons for this will be discussed later.

The role of competitive understandings. The interdependence of action, which exists because of the competitive environment in most markets, tends to lead to competitive understandings among dealers on both prices and trade practices. Where such a situation exists, there is considerable risk that dealers may agree among themselves to maintain or to raise their selling prices, to discourage entry of new competitors, or to take other kinds of action to protect and advance their mutual interests.

It is difficult to distinguish between fair and effective competition that is in the public interest and unfair and destructive competition which is not in the public interest. The competitive understandings that develop in the milk distribution industry may create a framework for orderly marketing which is conducive to fair and effective competition. However, they may go further and provide the basis for excessive profits to participating firms, at least in the short run.

Non-price competition. As noted, price is only one means by which milk dealers compete. A dealer also may engage in various forms of non-price competition which help him to pre-empt a share of the market and thus to increase his sales and possibly his share of the total market. Milk dealers seem to prefer non-price forms of competition to price competition because these forms are less easily duplicated by others.

Tendency toward price competition and instability. Although some of the basic elements in the competitive environment tend to price leadership and to the avoidance of overt price competition among established distributors, a "live and let live" policy is difficult to maintain under present conditions. Established milk dealers in most markets are finding it more and more difficult to avoid outright price competition.
The rapidity of technological change and innovation in distribution practices and methods and the existence of unused capacity coupled with the high fixed costs of operating processing plants and distribution routes apparently have been important causes for the increased intensity of price competition. Other contributing factors include: 1) the lack of significant brand preference for milk; 2) the importance of milk to consumers; 3) the variation in number, size and preferences of buyers; 4) the perishability of the product; and 5) the variation in types and interests of distributors. These forces tend to encourage price competition among dealers and sometimes result in retaliatory price cutting. In some markets, retaliatory price cutting at times has resulted in a downward spiralling of prices to such low levels that even efficient, low-cost firms cannot break even.

Competitive behavior among established dealers seldom takes the form of reducing prices to all buyers in the usual types and sizes of containers. It more often takes the form of granting discounts to selected buyers. Buyers differ widely in their demands for services, bargaining power, and in their responsiveness to price. List prices, where used, are often set at levels which distributors think are the maximum they can charge small volume buyers such as neighborhood stores. Price concessions commonly are granted to larger-volume customers and to those who are prepared to accept less service.

For pricing purposes, distributors, consciously or not, tend to group customers on the basis of demand differences. By recognizing the varying demands among customers and charging different prices to different customers (which may or may not be justified by cost differences), a distributor hopes to obtain fuller utilization of his facilities, spread fixed costs over a larger volume and increase profits. The fact that the unit costs of operating milk plants and distribution routes increase rapidly when plants or routes fall below capacity generates strong pressures to maintain or increase volume and thus for price

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2/ Fluid milk is a bulky, highly perishable, and easily contaminated food that must be marketed expeditiously, with little opportunity for storage. These conditions severely limit the alternatives of both dealers and producers as to the time and place of sale.
The success of charging different prices to various customers depends in part on the concealment of price concessions from other customers for as long as possible. Success also depends, in part, on whether or not the firm receiving the concession passes on the reduction to its customers.

For these reasons, "off-list" pricing (i.e., pricing which includes unpublished and individually negotiated discounts) is a common practice in dealing with large food stores as well as with other types of customers. Dealers believe that this practice helps them to hold their present customers and at the same time to obtain new accounts. A distributor may grant price concessions to large stores, if demanded, to avoid losing a major account to a competitor. This is especially true when dealing with food chains that have attractive alternative sources of supply, including the possibility of establishing their own delivery routes and processing plants.

The price concessions used to obtain and to hold desirable store customers may take various forms including: cash discounts, cash payments for future patronage, liberal credit, loans, advertising allowances, and provision of refrigeration equipment without charge or below cost.

The struggle among milk dealers to serve an important account may become a competitive battle that leads to retaliatory actions by competitors and ultimately to a price war. Dealers are especially concerned with price cutting in any form by "volume-hungry distributors" to capture the business of supplying supermarkets.

The rapid pace of technological change and innovation in the transportation, processing and distribution of milk has been an important factor making the competitive environment more conducive to price competition and to the disruption of price stability. The changes in marketing practices required to keep pace with developing technology strains competitive understandings among dealers.

Open price competition often is associated with the introduction of new distribution techniques. The development of specialized dairy stores in many New England and Ohio markets and more recently on Long Island has resulted in

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Fixed costs (i.e., those items of expense which remain unchanged with a change in plant volume) usually constitute a larger proportion of total costs in small plants than in large ones. In an analysis involving four model plants, nearly three-fourths of the expense in the smallest plant (capacity of 1,220 quarts a day) was fixed compared to less than one-third in the largest plant (capacity of 19,397 quarts a day). (M. C. Conner, F. C. Webster and T. R. Owens, op. cit., page 59.) A case study of three distributors in large upstate New York markets indicated that nearly 70 percent of the costs of operating a retail milk route were fixed. (Unpublished data of G. T. Devino and R. D. Aplin, Department of Agricultural Economics, Cornell University, Ithaca, New York.)
major price reductions. In these situations the price reductions appear to be largely, if not entirely, a reflection of the potentially lower costs that can be achieved by this new method of distribution. But even where price reductions are motivated by gains in efficiency, they temporarily may exceed the cost savings that can be achieved.

The attempt by a dealer to expand his operations into a new market may lead to price instability. Frequently a milk dealer enters a market by acquiring an established business and expanding it. The increasing advantage of large-volume processing plants, the use of improved paper containers, improved roads, new delivery labor arrangements, more uniform sanitation standards and the like, have increased the area that can be served from a single plant. It is now more feasible, economically, for a dealer to enter a new market without buying an established business. This has been an added reason for price instability except where prevented by the restrictive licensing policy of the Department of Agriculture and Markets.

A milk dealer may try to gain customers in a new market by offering added service, promotion devices or other non-price concessions. On the other hand, a dealer may gain entry into a market by appealing to customers through reduced prices. In recent years, some dealers in trying to establish themselves in a new sales area have used special methods of distribution such as dairy stores, limited-service delivery and vending machines.

The success of a dealer in establishing his business in a new area depends on how quickly and to what extent other distributors adjust their prices. Usually, competing distributors reduce their prices to hold or recapture customers. This often results in further cuts by the new entrant and on some occasions has resulted in severely depressed prices. Eventually, however, prices tend to increase sufficiently to enable at least the more efficient distributors to operate profitably. The firm that introduced the innovation and initiated the price cutting may become, after the new situation has stabilized, a strong conformist to the new price structure in the market, even defending it against challenges by other firms.

Another condition that leads to price instability in markets is the existence of a surplus of available fluid milk supplies. This situation coupled with the lack of other profitable alternatives for using the milk may cause country suppliers to sell milk to fluid dealers at depressed prices even though minimum prices for Class I milk are fixed by federal or state orders. Such “distress” supplies may be offered for less than the actual costs of the milk, handling and transportation. This situation affects various dealers differently. It gives a competitive advantage to those who do not own country facilities. This situation results not only in providing some dealers with larger margins within which to operate but also may increase the number of alternative sources of milk for some of their subdealer customers. Although the tendency for supplies of market milk to outrun the demand at times has been a factor contributing to price instability in some instances, marketing orders have removed much of the variation in the cost of raw product to dealers that would exist otherwise.
In summarizing the general nature of competition among milk dealers, it should be stressed that several elements exist in the fluid milk distribution industry that make it susceptible to intense price competition, occasional price wars and other destructive practices. In addition to the basic factors that have been described, the human element exists. Price cutting, once underway in a market, occasionally leads to "emotional pricing" by some individuals. Then a price reduction may become an irrational action which reflects the feeling of a distributor who says "I've had enough," "I'll show them," or "I'll bring this situation to a head." There can be no question that this element has contributed to some degenerative price battles in the dairy industry.

In the past, the difficulty of maintaining price stability and avoiding destructive price competition has led dairy processors, distributors, and producers in individual markets to attempt to block entry of new firms in various ways. For instance, health regulations have been established by some state or municipal authorities to favor milk locally produced or processed. In some instances, state and local laws or regulations have prohibited the adoption and use of multiple-quart containers. The sale of some types of fluid milk products (e.g., low-fat products) and the use of new methods of distribution (e.g., milk dispensers) have not been allowed in some areas. Restrictive licensing of milk dealers also has been used to limit entry in New York, Virginia and perhaps other states.

Although such institutional barriers have become less prevalent and less effective since World War II, they still insulate some markets to a considerable degree from the adoption of new techniques and the entry of additional competitors.

**Competition Among Food Stores in the Sale of Milk**

The last few years have witnessed a sharp drop in the number and importance of small food stores and a large increase in the number of supermarkets. With more and more milk being sold by supermarkets, they have become an increasingly important element in the competitive structure of fluid milk markets in New York State and other areas.

Fluid milk has become an important sales item for most food stores. It is a high turnover item and, as such, can be a profitable item with a relatively low mark up. Moreover, milk is considered by some store operators to be a good traffic builder because it is an item that is purchased frequently by consumers, is widely used, cannot be stored long by consumers, and is a rather homogeneous product with relatively little brand differentiation.

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1/ For the definition of the term "destructive practices" as used by the Committee, see page 29.

In most areas, supermarkets are accessible to more consumers than in the past. The size of the trade area served by individual supermarkets has increased because of increased consumer mobility. Moreover, supermarket capacity has been increasing faster than population growth for more than a decade. In recent years, added pressure has arisen in some areas from the entrance into the food business of large discount houses that have established cut-rate food outlets. These factors have intensified the competition among supermarket operators.

Until recently, supermarkets were able to grow and increase their earnings by absorbing much of the business formerly done by small neighborhood grocery stores. Now that most of the potential expansion by this means has been achieved, supermarkets must seek increased volume largely by competing among themselves. Moreover, voluntary chains of independent supermarkets have succeeded in offering strong competition to corporate chains. This development has added to the intensity of competition among supermarkets. In view of these factors, as well as others, many operators of large food stores are striving to achieve lower in-store costs and lower-into-store prices of products, including milk, to widen their margins and improve their earnings.

Another element that is important in explaining the nature of competition among food stores is the cost structure of supermarkets. As in the case of milk dealers and many other businessmen, a substantial part of the costs of operating a store are fixed in the sense that they do not change appreciably with changes in volume, either upward or downward. A recent study made by a firm of management consultants for the General Foods Corporation indicated that about 43 percent of the total expense of a typical supermarket (exclusive of costs of products) is fixed. The high fixed costs of operating stores make the sales volume per store very important to the store operator.

Under these conditions, although food store operators want an adequate margin on milk, they are even more concerned about pricing milk low enough to hold the customers they have and if possible to gain additional ones. Most operators of supermarkets apparently think that they cannot afford to have a competing supermarket sell milk at a lower price. Moreover, they know that nearby stores probably will meet promptly any cut they may make in the price of milk. Consequently, store operators frequently follow a "live and let live" policy in pricing milk for rather long periods of time. Some supermarkets apparently have taken relatively wide margins for rather long periods of time. Yet from time to time cuts are made in milk prices, just as in the sale of other items. Some supermarket chains on occasion have decided to feature milk, promoting it with intensive advertising and merchandising at prices lower than would be required to yield a normal profit.

Concluding comments on nature of competition. Several attributes of the fluid milk distribution industry tend to make it more susceptible than it formerly was to intense price competition and to occasional price wars. In recent years, with the rapid pace of technological change and innovation, retail prices of milk have exhibited less evidence of industry control, either through price leadership or mutual agreement.

Specialized, limited service distribution systems have resulted in reduced retail milk prices and distribution margins in many markets in recent years. Dealers contend that while these specialized types of distribution are low cost operations, they serve only a small segment of the market and can make other methods of distribution (e.g., home delivery) unprofitable to the point of eventual elimination. The dealers, therefore, question whether the expansion of low-cost, limited service types of distribution through unrestricted price competition is in the public interest. The Committee is impressed, however, with the fact that the specialized, low-cost systems of distribution tend to bring long-run gains in efficiency and to make milk available, especially to low-income families, at prices consistent with the limited services offered. It believes that these advantages outweigh the possible adverse effects on more costly systems of distribution. Thus the Committee concludes that the development of specialized, limited service distribution systems is in the public interest.

The increased variability in retail milk prices that has occurred in recent years is disturbing to the industry but on the whole it gives greater assurance that benefits of the competitive system of distribution will be reflected promptly to consumers and producers. It is important from the viewpoint of the public interest that government regulation not interfere with the adoption of more efficient practices and low-cost methods of distribution.

**Impacts of Technological Change and Price Wars**

A careful examination of the impacts of rapid technological change, intense price competition and price wars is an important step in evaluating the need for regulation of competition in the fluid milk industry and in the choice of regulatory measures.

Milk dealers who conferred with the Committee expressed concern about outbreaks of price cutting that sometime degenerate into ruinous price wars. They view such price wars as a cause of heavy financial losses and a threat to their survival. They also contend that price wars are harmful to producers and consumers as well as to milk dealers and their employees. More specifically they contend that legislation is necessary to prevent the following:
1. Ruinous losses to dealers, driving many of them out of business, and thus promoting a trend toward monopoly.

2. Losses to producers through failure of inadequately bonded dealers and the inability of dealers to pay customary handling charges and premiums over minimum order prices.

3. Further curtailment and possible elimination of home delivery with consequent adverse effects upon the sale and consumption of fluid milk and by-products.

Especially cited by the dealers in support of their position were the 1962-63 price wars on Long Island and recent ones in Buffalo and New England. Price cutting to capture the business of chain supermarkets and the sale of milk at sharply reduced prices by specialized dairy store operators were most feared by the dealers. The failures of the Whiting Milk Company in 1960 and Norwood’s Superettes, Inc. in 1963, both in New England, with substantial losses to producers and cooperatives were mentioned repeatedly as evidence of the need for protective legislation.

The Committee considered carefully these concerns of the dealers in analyzing the probable impacts of price wars on the various interested groups, which constitute the “public interest”.

Effects on Milk Distributors.

There is no doubt that the rapid pace of innovation, outbreaks of intense price competition and retaliatory price cutting have serious impacts upon milk distributors. Although some distributors benefit from these developments, others are seriously disadvantaged. The incomes of established distributors are reduced to varying extents depending upon the kind of trade served and upon the dealers’ abilities to reduce costs and to hold or build volume.

A dealer with limited financial resources who is dependent upon earnings in a single market may be forced out of business by an extended price war even though he is relatively efficient. On the other hand, dealers with sufficient resources to weather a period of intense price competition, who are able to lower costs and to maintain or expand volume, may achieve long-term gains. Distributors with operations in several markets may be in a comparatively favorable position, if losses in one market can be compensated for by profits in other markets.

Intense price competition stimulates distributors to reorganize their operations so as to process and distribute milk successfully even with reduced margins. Some firms have had outstanding success in reorganizing operations during periods of intense price competition.
In periods of keen price competition and rapid technological change, some firms are forced out of the dairy business either through poor management, inadequate financial resources or heavy dependence on a particular method of distribution that is adversely affected. The number of processors and distributors in New York, as well as in other states, has decreased over the years. This has not been due primarily to destructive competition but to the technological and other changes described earlier. Undoubtedly the number of processing plants and the number of distributors in New York will decrease further. Unfortunately, many dealers whose businesses represent their lifetime efforts will find their earning power drastically reduced and their assets impaired as new marketing methods and practices develop. This is not a new condition, however, and is not unique to the dairy industry.

Similarly, not all store operators are affected in the same way by intense cutting of milk prices. Some store operators are successful in obtaining price concessions from their milk suppliers. Small neighborhood storekeepers, however, may be seriously hurt by severe price competition. They have little opportunity of expanding their sales volume enough to compensate for the reduced margins, and yet they cannot afford to lose customers by holding the line on milk prices. On the other hand, some supermarket operators view milk as a traffic builder and can increase sales through reduced prices of milk and thus receive positive benefits over time, if not immediately. Moreover, since milk is only one of several thousand items sold by a supermarket, reduced milk prices do not reduce the stores’ overall margins very much as compared with milk dealers who are dependent upon milk for the major part of their income.

The operators of specialized dairy stores characteristically appeal for business through low prices. Experience indicates that well managed dairy store firms have grown during periods of intense price competition.

Effects on Producers

A majority of the farmers in New York State depend upon milk for a large part of their income. For many, milk is practically the sole source of income. A strong, expanding milk industry, therefore, is of great importance to the farm and rural economy of the State.

Producers realize both beneficial and harmful effects from price wars among milk dealers. The benefits come from the increased sales of fluid milk induced by lower retail prices. Milk consumption tends to increase from two to four percent for each 10 percent reduction in price. Moreover, potential lower cost substitutes for fluid milk such as concentrated, sterile and powdered milks and

products in which vegetable oils replace milkfat are being aggressively de-
veloped. The availability of more acceptable substitutes would make the sales
of fluid milk more responsive to price changes than heretofore.

Lower retail prices that result from vigorous competition encourage the
introduction of new low-cost methods and practices. Cost reductions tend to
protect the fluid milk market by strengthening its ability to compete with low-
cost substitutes. The loss of part of the fluid market through failure to make
this product available to consumers, especially the lower income groups, at the
lowest prices possible, would be highly detrimental to producers, as well as to
many distributors.

Sales gains resulting from intense competition and lower prices may be off-
set in part by the reduced availability and convenience of milk if home delivery
gives way to sales through supermarkets and dairy stores. Moreover, some
milk dealers who are hard hit by price wars may give less support to promo-
tional programs for maintaining and increasing the sale of milk.

Before marketing orders came into general use, losses suffered by milk
dealers during periods of intense price competition often were passed back to
producers in the form of lower milk prices. Now that minimum prices paid by
dealers for fluid milk in most areas are determined by federal or state market-
ing orders, producers are protected to a large degree from any pass-back of
dealer losses. Occasional losses may result from the failure of dealers who
cannot pay for the milk they have purchased from producers. Such losses have
occurred infrequently, however, even in areas like New York which have no
resale price regulation and only limited regulation of trade practices. Recent
changes in the bonding provisions of the New York Milk Control Law empower
the Commissioner of Agriculture and Markets to require a dealer to pay into an
escrow fund to help insure producer payment when his business appears to be
financially weak.1/

Reduced margins in distribution due to price wars reduce income to operat-
ing cooperatives and hence to their producer members. In addition, during
periods of intensified price competition, dealers are likely to reduce or elimi-
nate premiums over minimum order prices that would otherwise be paid to
individual producers and to reduce the amount they will pay cooperatives in the
form of handling charges. However, the general supply-demand situation for
milk, rather than price wars, is the major factor which determines the extent
and amount of premiums and handling allowances which exist at a given time.

Another potential disadvantage of price wars to producers, in the long run,
is the possible impairment of the market structure to the extent that the com-
petitive vitality of the industry is reduced. This danger is discussed on suc-
cceeding pages.

1/ Section 258-b, Article 21, New York State Milk Control Law.
On the whole, it appears that producers are likely to gain more than they lose from essentially unregulated competition among milk dealers.

Effects on Consumers

In the short run, at least, consumers benefit from the low prices that result from intense price competition. If such competition stimulates dealers and store operators to adopt improved methods, or more economical systems of distribution, benefits to consumers may continue indefinitely.

On the other hand, some consumers may be adversely affected by severe price competition. For example, milk may become less conveniently available, especially to consumers who need or prefer home delivery. Consumers also may have a more limited choice of brands, container types and sizes, and fewer services as the result of price wars and severely reduced margins.

Severe and persistent price wars may cause milk processors and distributors to give less attention to practices and conditions that contribute to the maintenance and improvement of quality. Dealers may be forced to curtail expenditures for quality control even though minimum sanitary standards are protected by health regulations.

The major disadvantage of price wars, both to consumers and producers, in the long run, is the possible impairment of the market structure to the extent that the competitive stimulus for firms to provide good products and service at reasonable prices is reduced. It is possible that uncontrolled price competition over time might reduce the number of distributors in a market to the point where the competitive vitality of those remaining is seriously curtailed. Unfortunately, the point at which competitive vigor is likely to disappear from a market and monopolistic tendencies likely to prevail cannot be predicted.

A decrease in the number of firms in a market does not necessarily mean that competition will be less effective. If the reduction is drastic enough, however, the limited number of milk distributors remaining could be in a position of market control. Useful marketing services might be curtailed and consumers might have a more limited choice of sources of milk. There would be greater danger that prices would be arbitrarily enhanced. There would be less assurance that improvements in marketing efficiency would be made, and if made, that the gains would be shared with either consumers or producers.

Unfortunately, it is difficult to assess whether or not unrestricted competition will lead to such harmful results. So far there is no clear indication that such results are near at hand. The further elimination of licensing restrictions to entry would reduce the likelihood of monopolistic abuses developing. This risk, however, should not be ignored. Once competition has been reduced to a point of inadequacy, it may be difficult to restore. The alternative then becomes direct government intervention with regulation of services and prices.
Congress, as well as many state legislatures, in the enactment of antitrust laws and trade regulation acts, has officially recognized the possibility that unrestricted competition may “substantially lessen competition and tend to create a monopoly”. To protect the public interest, Congress has conferred authority upon appropriate agencies to prevent or control competitive practices that may have such results.

Effects on Dairy Employees

Many of the developments taking place in milk distribution pose serious problems to many persons employed in milk distribution and to their unions. Reduced incomes or losses suffered by milk distributors as the result of price wars are reflected in less favorable employment opportunities for labor. Under the pressure of reduced incomes or losses, milk dealers respond less favorably to union demands for higher wages, larger fringe benefits and shorter work weeks. Firms that employ non-union labor tend to gain at the expense of those operating under union contracts.

Some of the important changes in milk distribution which affect price competition are being made to reduce labor costs. Certain labor contract provisions limit the ability of management to adjust to changing conditions. Thus, existing labor arrangements may stimulate a greater decline in the number of employment opportunities in the long run than if such rigidities did not exist. Labor may have a brighter future in an efficient industry that adjusts rather promptly to new technology than in one which lags seriously in making needed changes.

Destructive Competition

As noted, price competition such as now prevails and is likely to prevail in the absence of further regulatory action, has both beneficial and harmful effects upon the several groups that constitute the public interest. Intense price competition and retaliatory price cutting may force prices and margins so low as to cause serious hardship for many milk dealers and their employees. On the other hand, consumers and most producers appear to benefit from these developments at least in the short run.

The process of adjustment to changing conditions, painful as it is to many, is likely to continue indefinitely, whatever may be done in the way of regulatory action. Most of these hardships are inescapable in a competitive system. Competition in pricing as well as in marketing services is an essential part of the competitive system under which the major part of the economy operates. It provides the stimulus for increased efficiency and for the adoption of improved, more economical methods of distribution, to the ultimate benefit of consumers, producers and many of the marketing agencies. Nevertheless, the Committee is concerned about the continuation of certain destructive practices in the industry that develop in the competitive environment that now exists in New York State.
"Destructive competition" has a wide range of meanings. The Committee uses this term to mean practices that "tend to impair the market structure". By "impairment of market structure" is meant the elimination or weakening of efficient firms in a market with the ultimate result that needed marketing services are likely to be curtailed or marketing margins unduly enhanced. The latter may occur because innovations and the adoption of more efficient methods and systems of marketing are discouraged, or by the arbitrary determination of prices by a dominant dealer or group of dealers when effective competition has been suppressed.

In the Committee's opinion the most serious destructive practices involve the sale of milk at unreasonably low prices (which the Committee defines as prices so low as to make the position of efficient, low-cost competitors untenable) and unwarranted price discrimination in the sale of milk to different customers or in different sales areas. These practices, when carried to the extreme, violate accepted principles of equality of opportunity. They may involve the exploitation of inequality in bargaining power and economic strength without regard to efficiency. They are contrary to the fundamental precept of a private enterprise economy that consumer choice and the economic efficiency of firms in responding to this choice, rather than economic power, will determine which firms survive and grow and which will not.

It is difficult to distinguish between competition that is really unfair and destructive in the sense that it is harmful to the public interest, and that which is beneficial to that interest, even though it may be distasteful or injurious to some firms that cannot compete successfully. This is true especially in a time like the present when consumer's preferences for the various products, packages and methods of distribution are changing rapidly and when new technologies and distribution methods are having a pronounced impact upon marketing practices and the size of business required to achieve low unit costs.

Part II

Legislative Remedies for Destructive Price Cutting and Other Unfair Practices

A Brief Historical Review

Abuses of the competitive system not only in regard to milk but in the business world generally have been a matter of public concern for centuries. It will serve our present purposes merely to trace the development of legislation on this subject briefly from the enactment of the Sherman Anti-Trust Act of 1890 to the present. The Sherman Act was directed primarily toward the control of monopolies and restraint of trade. Other federal laws designed to elaborate
and perfect such control and also to curb unfair methods of competition, fol-
The Clayton Act condemned monopolistic practices such as price discrimination 
that tend “to substantially lessen competition or to create a monopoly”.

A later amendment to the Clayton Act, known as the Cellar-Kefauver Law of 
1950, more explicitly forbids corporate mergers and acquisitions where the 
effect will be substantially to lessen competition or tend toward a monopoly.

Meanwhile most of the states also adopted legislation for curbing abuses of 
competition in intra-state commerce, with emphasis on prohibiting many prac-
tices that were declared to be unfair and destructive.

Interest in regulating competition both nationally and at the state level was 
stimulated during the period of severe economic depression in the 1930’s. The 
National Industrial Recovery Act of 1933 authorized, among other things, the 
promulgation of industry trade practice codes.

In 1936, Congress showed its continuing concern with trade practices that 
lessen or destroy competition, by adopting the Robinson-Patman Act. This law 
amended the Clayton Act, more explicitly prohibiting price discrimination and 
the giving or receiving of discriminatory allowances or rebates.

The Miller-Tydings Law of 1937, which amended the Sherman Act and the 
Federal Trade Commission Act, authorized manufacturers to require distrib-
utors of their branded products to sell these products only at specified prices. 
Many of the states, New York included, enacted similar laws.1/ In 1952, after 
the Miller-Tydings Act was declared unconstitutional by the Supreme Court, 
Congress enacted the McGuire-Keogh Fair Trade Enabling Act. This law made 
it possible for manufacturers to enforce their resale price maintenance con-
tracts on non-signers in any state where such contracts were legal. However, 
in an increasing number of states such laws have been invalidated by the Courts.

For a time, resale prices of many branded products as sanctioned by these 
laws were rigidly maintained. In recent years, however, this system of price 
maintenance has broken down in many states under the impact of unfavorable 
court decisions, popular criticism, the competition of unregulated brands, and 
the development of the discount house.

The difficult economic situation of the early 1930’s stimulated an insistent 
demand by milk producers and dealers for protective legislation. In response

1/ In at least one instance, milk dealers (in Phoenix, Arizona, 1961-62) attempt-
ted to use such legislation as a basis for fixing the prices at which their 
registered brands of milk could be sold by stores. The attempt failed when 
a prominent supermarket operator obtained an unregulated supply from an 
outside source.
to these demands, between 1933 and 1936 or thereabouts, many states adopted milk control laws which authorized milk control boards or similar agencies to fix minimum retail and wholesale prices of milk, to regulate trade practices of milk dealers and to fix prices at the producer level. New York State was the leader in this movement. Its emergency milk control law, adopted in 1933 following a legislative committee investigation, was widely copied by other states.

For a time in 1933-34 resale prices of milk and trade practices in the distribution of milk were regulated by federal milk marketing agreements. However, the federal government soon abandoned this controversial effort, and has since limited its regulation of milk prices to the producer level only.

Economic recovery during the late 1930's and the change from prewar surpluses to wartime shortages during the 1940's brought a lessening of interest in regulatory measures to restrain competition. A number of states, including New York, that had undertaken the regulation of resale prices and trade practices abandoned this policy. It should be noted, however, that the abandonment of resale price regulation by some states was due in part to the substitution of federal control for state control of producer prices in their jurisdictions. (Protection of producer prices and income had been a major reason for undertaking the regulation of resale prices by the several states.)

During the last decade there has come a new wave of interest in legislation designed to prevent destructive price cutting and unfair trade practices in the sale of milk at retail and wholesale. The renewed demand for such legislation has been stimulated by disruption of established price structures and trade relationships as a result of the dynamic changes in handling, processing, packaging and distributing milk described in Part I. The tendency for supplies of market milk to outrun the demand, causing troublesome surpluses also has been a factor.

In response to these conditions a number of states have adopted new legislation for curbing destructive practices in milk distribution. Two states (New Jersey and Florida) have reinstated price control regulations that had been suspended previously. As explained later, many states have general laws pertaining to trade practices which apply to the sale of milk and dairy products as well as to other commodities.

Present Regulation of Milk Distribution in New York State

In New York State there is at present no regulation of retail or wholesale prices of milk and relatively little regulation of trade practices in the distribution and sale of milk, aside from a) sanitary requirements, and b) marketing orders and other regulations which pertain to dealer purchases of milk and payments to producers. To a limited extent, however, existing New York State and federal statutes provide for some regulation of competition in the industry.
Article 21 of the Agriculture and Markets Law grants broad general powers to the Commissioner to supervise and regulate the entire milk industry, including the distribution, delivery and sale of milk as well as its production, transportation and storage. The Commissioner is authorized to investigate all matters pertaining to these activities and in connection therewith to subpoena milk dealers and their records. He is also authorized to act as mediator and arbitrator in any controversy between milk dealers or between dealers and producers.

In addition, Section 258-c of Article 21 gives the Commissioner some authority to deal with trade practices of milk dealers in connection with the granting and revoking of licenses, which are required as a condition of engaging in business as a milk dealer. He is authorized to refuse to grant or renew a license to a milk dealer, and likewise to revoke the license of a milk dealer, who “has committed any act injurious to the . . . public welfare, or to trade or commerce in demoralization of the price structure of pure milk to such an extent as to interfere with an ample supply thereof for the inhabitants of the state . . .” (Underlining added.) He may also refuse to grant or renew a license to a dealer, and may revoke the license of a dealer, who “has continued in a course of dealing of such nature as to satisfy the Commissioner of his inability or unwillingness properly to conduct the business of receiving or selling milk or to satisfy the Commissioner of his intent to deceive or defraud producers or consumers”.

A further provision with respect to licensing is that the Commissioner may deny a milk dealer license to an applicant if he finds, by a preponderance of evidence, “that the issuance of the license will tend to a destructive competition in a market already adequately served”.

In general, the authority granted to the Commissioner to regulate trade practices of milk dealers has been used with much restraint since resale price fixing was discontinued, in 1937. So far as is known to the Committee, no milk dealer has had his license revoked because he engaged in unfair or destructive trade practices. Presumably the Commissioner has not attempted to use his authority in this respect because the possibility of showing in any instance that the price structure had been demoralized to the point of interfering with an ample supply of pure milk to the inhabitants of the state is remote.

On the other hand, the authority granted to the Commissioner of Agriculture and Markets to refuse to grant a milk dealer license or to extend an existing license to additional territory, on the ground that it might contribute to destructive competition in a market already adequately served, has been used to significantly limit competition among milk dealers in New York State.

In the report of a study of state milk control programs in 1955 it was stated:1/

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"The primary purpose of restrictive licensing of milk dealers and plants is to prevent destructive competition such as severe price cutting and price wars. In New York State, where there is no direct control of resale prices, restrictive licensing is especially relied upon as a means of safeguarding the industry from such occurrences."

Restriction of license extensions probably has limited competition fully as much as the policy of issuing new licenses sparingly. Milk dealers (and plants) have been licensed to operate in prescribed areas and have not been permitted to extend their operations without having their licenses amended.

Though still somewhat restrictive, licensing policy has been liberalized to a considerable extent in recent years. A significant step in this direction was taken in 1957 when counties were recognized as natural marketing areas for purposes of licensing. This means that a milk dealer having a license to operate in any part of a county may extend his operations throughout that county without the necessity of having his license amended. New licenses also are believed to be granted somewhat more freely now than was the case earlier.

The policy of restrictive licensing of milk dealers in New York State has evoked a great deal of criticism and controversy. In 1959, Governor Rockefeller appointed a Special Committee on Milk Licensing headed by Dr. Everett Case who was then president of Colgate University. In its report that Committee stated among other things:

"The Committee is aware that in recent years the Division of Milk Control has moved, by the exercise of administrative discretion, toward the objective of freer entry into the industry. . . . The Committee is aware also of the recent liberalization of territorial restrictions in licensing which has tended to provide freer entry into markets. . . . During the past several decades, technological developments in the industry, improvements and expansion of the State’s system of roads, and the pattern of population expansion have created market situations in which territorial restrictions on licensing could act as deterrents to the adoption of cost-reducing innovations by the industry . . . While the record of the Division in approving . . . applications for license extensions. . . cannot be ignored, any attempt to limit competition by means of licensing is not, in the Committee’s opinion, a proper objective of licensing. . . . To deny to dealers, either

legislatively or administratively, equality of opportunity to compete fairly with dealers already serving a market can delay or prevent producers, dealers and consumers alike from realizing and sharing in the full rewards of economic enterprise and initiative."

The Case Committee went on to recommend certain changes in the Milk Control Law designed to give greater assurance of free entry to the business of distributing milk and to facilitate expansion of existing businesses into new territory. The Committee coupled its recommendation for a liberalization of restrictions, in licensing with recommendations for preventing destructive trade practices.1/

The implementation of the powers other than licensing granted to the Commissioner of Agriculture and Markets to deal with destructive competition has been limited mostly to occasional investigations of price war situations and private hearings or conferences pertaining thereto. Such investigations were conducted in the New York City Market in 1950-51; in Rochester in 1960; and on Long Island in 1960 and again in 1962-63.

Milk dealers are, of course, subject to the General Business Law of New York State as well as to the Milk Control Law. Articles 340-347 of the General Business Law of New York State, commonly referred to as the Donnelly Act, constitute New York’s principal antitrust law. The Donnelly Act, which was enacted in 1897, was directed toward the control of monopolies and restraints of trade and pertains to the same types of economic activities, in intrastate commerce, as the Sherman Anti-Trust Act of 18902/ does with respect to interstate commerce.

The Donnelly Act forbids “every contract, agreement, arrangement or combination . . .” 1) which establishes or maintains, or may establish, a “monopoly in the conduct of any business, trade or commerce or in the furnishing of any service” in the State of New York, or 2) which restrains or may restrain competition, or 3) whereby “for the purpose of establishing or maintaining any such monopoly . . . in the conduct of any business, trade or commerce . . .”, the free pursuit of business activity may be restricted.

Section 16 of Article 2 of the New York State Agriculture and Markets Law authorizes the Commissioner to “investigate restraints of trade or unlawful combinations to fix prices”.

1/ Ibid., pages 10-17.
On several occasions the Attorney General of the State of New York has investigated alleged complaints of violation of the Donnelly Act by milk dealers and their trade associations. Some of these investigations have resulted in obtaining judgments against the alleged violators.

New York State has no law which serves as a counterpart to the Clayton Act, as amended by the Robinson-Patman Act, which bans discriminatory pricing in interstate commerce.

Kinds of Regulatory Programs for Dealing with Destructive Competition in the Sale of Milk

The task before us is to determine insofar as possible what form of new regulatory power is desirable, and what extent of regulation would now be most appropriate, and whether or not the social gains from such a program would significantly outweigh the disadvantages and costs involved. In attempting to answer these questions the Committee has studied the problems of competition which confront the milk industry of this State. It has given serious consideration to the views of milk dealers as well as to those of the leaders of milk producer organizations. It has also studied the experience of New York and other states with the various kinds of regulatory programs that have been used to deal with such problems. In addition to the first-hand information about these programs supplied by certain of its members, the Committee has examined much published material on the subject. It has also had the benefit of consultation with competent persons having intimate knowledge of the various regulatory programs and their effects.

The regulatory programs for dealing with destructive competition among milk dealers that have been tried in New York and other states cover a wide range. For convenience of discussion and analysis the Committee has grouped these varied types of regulation into four major categories, as follows:

1. Fixing of minimum resale prices of fluid milk (and fluid milk products) at all levels.

2. Prohibiting the sale of milk at unreasonably low prices.

3. Prohibiting unwarranted price discrimination and regulating other trade practices.

4. The fact-finding and educational approach, including investigations, trade conferences, educational programs, publicity, public hearings, and the like.

\[\text{1/} \text{ A list of reference material used by the Committee is given at the end of the report.}\]
The several types of regulation listed are, of course, not self-contained or mutually exclusive. Practically all state regulatory programs have embraced elements of two or more of the four categories. Some additional forms of regulation that have been used or might be used to deal with destructive competition in milk distribution are omitted from the foregoing list. The public utility type of regulation, which would involve the fixing of maximum prices and distributor margins as well as the regulation of marketing services, has not been used and probably would not be feasible or acceptable at this time. Regulatory procedures such as required filing or posting of selling prices by dealers, the use of cease and desist orders, and the licensing of milk dealers and stores are omitted from the list because they are considered to be, for the most part, not distinct programs in and of themselves, but rather devices for implementing the various kinds of regulation listed.

Criteria for Evaluating Such Programs

The purpose of any legislation to regulate competition in the sale and distribution of milk is to protect the public as well as firms in the industry from unfair competitive practices that interfere with the proper functioning of the system and threaten the survival of firms providing consumers with desired products and services in an efficient manner. The desirability of various regulatory programs that might be considered should be judged on the basis of the following three criteria:

First, the extent to which a given program would meet the problem of destructive competition and its probable effectiveness for that purpose.

Second, the extent to which such a program would facilitate adequate and effective competition and the prompt adoption of more efficient practices and low-cost methods of distribution.

Third, the feasibility of satisfactory administration and enforcement at reasonable cost.

To be acceptable, any program for further regulating competition in the sale of milk should offer promise of doing significantly more good than harm.

Fixing Minimum Retail and Wholesale Prices of Milk

Many states, including New York, have had experience with this form of price regulation. In 1963 minimum resale prices of milk were being fixed in 16 states, including five northeastern states: Maine, New Hampshire, Vermont, New...
Jersey and Pennsylvania. Other states that fixed minimum resale prices of milk in 1963 were Virginia, North Carolina, South Carolina, Georgia, Florida, Alabama, Louisiana, Nevada, Wyoming, Montana, and California. Altogether about 29 states have had some experience with regulation of resale prices of milk since 1933 when the first state milk control law was enacted in New York. Minimum resale prices were fixed in New York State for a period of four years, 1933-37. Nearly half the states that once regulated resale milk prices have discontinued it. A few states such as Nevada and Wyoming have undertaken such regulation recently.

As previously mentioned, minimum resale prices and trade practices of milk dealers also were regulated under federal milk marketing agreements in 1933-34.

Minimum resale price programs vary as to coverage in the various states. Most states that have such programs fix the prices at all levels, including retail, wholesale and dealer-to-dealer transactions. Some cover all or many fluid milk products sold by dealers, others cover fluid whole milk only. Exemptions commonly are granted for transactions pertaining to government contracts, and sometimes for milk sold to schools and other public institutions.

Criteria for establishing the minimum prices are, as a rule, stated in general terms in the various state laws, leaving much discretion to the administrative agencies. Most of these agencies have placed strong emphasis on costs as shown by evidence presented at hearings, sometimes supplemented by investigational findings. The margins established usually have been related to average costs for the market, including a "fair return" on investment, for periods in the recent past. The minimum resale prices established probably have been sufficient in most instances to enable all but the least efficient distributors to recover their total operating costs.

A tendency has been observed, in the states that fix minimum resale prices, to maintain small differentials or none at all between the prices charged for milk delivered to homes and the prices charged at stores for milk sold on a cash-carry basis, between one-quart, two-quart and gallon packages (on a per quart basis), and the like. In general, the fixing of minimum resale prices tends toward uniformity and rigidity, with strong ties to past conditions, customs, and experiences.

The prohibition of certain "unfair" trade practices has usually accompanied the fixing of resale prices. It has been considered necessary to prohibit practices such as free services, discounts, rebates and the like which tend to reduce the net charges below established minimums. Effective control of resale prices also requires that prices be specified for milk of particular types, grades and qualities. For example, higher prices are specified for milk exceeding a stated fat percentage, for homogenized milk and for milk fortified with vitamins or minerals.
Advantages

Comprehensive resale price fixing has a strong appeal to milk dealers, especially to those who have had no experience with the system and have found it difficult to compete in markets where prices are not fixed. If it were successfully enforced such a program would fulfill the first of the three criteria here-tofore enumerated, that of dealing directly with the problem of destructive competition. It would also give assurance of a stable price structure and tend to cushion the effects upon milk dealers of new technology and changing methods of distribution.

The fixing of minimum retail (and wholesale) prices has helped (within limits) to protect and maintain the system of home delivery thus benefiting large numbers of consumers who prefer home delivery, as well as the dealers who provide that type of service. Such consumers probably use more fluid milk than they would if they were deprived of the convenience and availability afforded by home delivery. On the other hand, as indicated below, price fixing no doubt has had an adverse effect upon milk purchases and consumption of milk by large numbers of people who would prefer to get the benefit of the lower prices that result from large-volume distribution through stores.

In addition to other considerations, this type of regulation has the advantage of definiteness. Every milk dealer is put on notice as to the minimum prices at which he may sell without incurring the risk of a penalty for violation. It also provides considerable protection to milk dealers from the risk of prosecution for price-fixing conspiracies, since the main responsibility for price determination is transferred to a government agency.

Disadvantages

Resale price control tends to create a pattern of price uniformity and rigidity, to maintain the status quo, and to discourage innovations and progress toward greater efficiency which the forces of competition otherwise would stimulate. There has been a tendency also to maintain retail prices at higher levels than necessary to cover the costs of the more efficient firms. Thus, this type of program has tended to protect inefficient high-cost operators.

The fixing of minimum resale prices as usually administered imposes a serious restraint upon the development of low-cost methods of distribution such as large-volume selling through supermarkets and dairy stores at low cash-carry prices. It tends to keep the retail prices of milk sold through such outlets at a higher level than would prevail in the absence of such regulation. This may more than offset the favorable effect upon consumption of maintaining a large volume of home delivery. The discouragement of low-cost methods of distribution under resale price control might ultimately affect the market for fluid milk very seriously by further aggravating the unfavorable price relationship between this product and competing substitutes.
Failure of milk control agencies to allow suitable price differentials for volume delivery and limited services to supermarket chains has led to a development in some areas of "captive dairies" and "captive supermarkets". Some supermarket and dairy store chains that have acquired their own processing facilities have been instrumental in bringing milk to consumers on a cash-carry basis at significantly lower prices and have contributed to more effective competition in milk distribution.

On the other hand, when such integrations occur primarily for the purpose of nullifying the impact of price control upon wholesale transactions between processing plants and stores, they are less likely to serve an economic purpose. Ultimately, such organizations may acquire enough market power to lessen competition, to the disadvantage of both producers and consumers.

Second, as shown by widespread experience over many years, the enforcement of minimum resale prices, particularly at the wholesale level, is very difficult and expensive. In addition to the effect of wide differences in unit costs among dealers the fixing of unrealistic prices and price differentials has aggravated the problem of enforcement. There has been widespread evasion and non-compliance with minimum wholesale prices, especially in large metropolitan markets. The result is that the regulations have not been applied equitably to all handlers. Ineffective enforcement has given encouragement to evasion and deceit.

Since compliance with minimum retail prices is usually much better than compliance with minimum wholesale prices, resale price control tends to result in abnormally wide margins but restricted sales volume for store operators. Wholesale distributors tend to receive relatively little benefit from this type of regulation.

In many of the areas where it has been tried, the regulation of resale prices of milk has been the subject of continuing and bitter controversy, and of much litigation. This has resulted in bad public relations for the whole industry as well as for the government agencies involved.

For the reasons indicated, the fixing of minimum resale prices of milk does not fulfill the requirements of the second and third criteria adopted by the Committee (page 36) as a basis for judging the acceptability of a regulatory program.

Lack of effective control of dealers' buying prices has contributed to the difficulties of enforcing minimum resale prices in some areas. But the problem persists even in markets where dealer buying prices are effectively regulated by federal orders.
Prohibiting the Sale of Milk
at Unreasonably Low Prices

Instead of fixing a complete schedule of minimum prices, some states have adopted or considered regulations prohibiting sales at unreasonably low prices. These regulatory plans exhibit much diversity. Several alternatives are noted as to the minimum allowable prices, namely:

1. The prevailing price in the market.
2. The average cost determined for similar transactions of representative dealers in the market.
3. The seller's cost, with the privilege of meeting a lawful price of any competitor.
4. A single basic floor price per quart at retail for whole milk (or minimum mark-up over the dealers' buying price for fluid milk established by a federal or state order).

Tennessee has attempted to prohibit the sale of milk below the prevailing price in a market (No. 1 above). Minnesota prohibits each dealer from selling for less than his cost but permits him to meet the lawful price of any competitor (No. 3 above). A few years ago proposed legislation that was given serious consideration in Connecticut but which did not become law would have authorized the control agency to prohibit the sale of milk below a specified floor price (No. 4 above). A similar proposal (as well as one in category No. 3) was offered recently by an Advisory Committee of Economists for consideration in revising the system of regulating competition among milk dealers in New Jersey. A bill passed by the New York Legislature in the spring of 1963 but disapproved by the Governor would have authorized the Commissioner of Agriculture and Markets to prohibit unfair and destructive practices on the part of milk dealers including the sale of milk at less than the average cost determined for representative dealers in a market (No. 2 above). Florida is now using this system along with resale price control.

This discussion will exclude consideration of regulations which prohibit selling below the prevailing price in the market or below the average cost of representative firms because these programs are very similar to the fixing of minimum resale prices, and the foregoing discussion of that type of regulation will apply. Our discussion will be centered on regulatory programs pertaining to the last two of the four definitions of unreasonably low prices given above, namely: first, prohibiting sales at prices below the seller's cost with the privilege of meeting a lawful price of a competitor, and second, prohibiting sales at retail below a specified floor price.
Prohibiting the Sale of Milk at Prices Below the Seller’s Cost With Privilege of Meeting a Lawful Price of a Competitor—The Minnesota Law

The milk control program of Minnesota is an outstanding example of those which undertake to prohibit the sale of milk below cost with the privilege of meeting the lowest legitimate price in the market. Consequently, it will be used here to illustrate that type of regulation. Later the same law will be used to illustrate the prohibition of unfair practices.

The original Dairy Industry Unfair Trade Practices Act of Minnesota was adopted in 1957. It was administered until 1961 by the Department of Business Development. In that year the law was amended and responsibility for administering it was transferred to the Commissioner of Agriculture. Prior to 1961, the law did not apply to manufacturers of dairy products. A companion law adopted in 1957, known as the “Loss Leader Prohibition Law” pertains to all types of business, but certain of its provisions are now incorporated by reference in the Dairy Industry Unfair Practices Act. It is this part of the Act which pertains especially to retailers, including stores. The Act, which in itself is very detailed, has been supplemented by an extensive list of rules and regulations. Products covered are milk, fluid milk products, frozen dairy foods and cottage cheese.

As the name suggests, this law prohibits a broad range of trade practices in the sale of milk. Among the prohibitions, is the provision that no manufacturer, distributor, wholesaler or retailer may sell, offer to sell, or advertise for sale, milk and specified milk products at less than cost—for the purpose or with the effect of injuring a competitor or destroying competition. This is the most important feature of the law. The banning of other practices evidently is designed principally to aid in the enforcement of the prohibition of selling below cost.

A significant requirement of the law is that each manufacturer, distributor, or wholesaler of milk and specified milk products must file with the Commissioner a dated schedule of his current wholesale prices, showing all applicable rebates, discounts and differentials. The wholesale distributor is required also to furnish the retailer with a copy of his current price list when negotiating a sale, and with all subsequent price lists.

All sales of such products must be made in accordance with the prices filed except “a sale made in good faith to meet a lawful competitive price”. The circumstances of any sales made at other than the filed prices must be reported to the Commissioner within five days. Such “deviated sales” may be made to government agencies, federal or state, and to public institutions, without being

1/ The fact that the Minnesota legislation is described here in some detail should not be taken to reflect an endorsement of this system of regulation by the Committee.
reported. Exemption also is provided for extraordinary situations such as liquidating an inventory or disposing of damaged goods. New price schedules must be on file for 10 business days before they become effective. The Commissioner may suspend for 10 days, pending investigation, any price filed by a manufacturer, distributor or wholesaler which he has reason to believe may not be in accordance with requirements of the law. The suspension may be extended for another 10 days.

Price schedules filed with the Commissioner are to be treated as semi-confidential, but any manufacturer, distributor or wholesaler may obtain information through the Commissioner about a competitor’s prices.

"Cost of doing business" or "overhead expense" is defined as all current costs including the following items of expense: labor (including salaries, and bonuses of executives and officers), rent, depreciation, selling costs, maintenance of equipment, delivery costs, all types of licenses, taxes, insurance, advertising and other fixed and incidental expenses. Nothing is said about an allowance to cover the use and risk of capital.

It is evident that a great deal is left to the discretion and judgment of the Commissioner in regard to the standards and procedure to be followed in determining the costs applicable to a particular product and type of transaction.\(^1\)

Any sale of milk or specified milk products by a retailer (store operator) at a price representing less than eight percent mark-up over his supplier’s posted price (or delivered invoice price or replacement cost) is to be considered

\(^{1}\) The California Milk Control Law is more explicit as to what is to be included in costs and as to methods of cost determination.

The Agricultural Code of California, Chapter 16, Article 2, provides that cost, as applied to manufacturers and distributors means the cost of raw product, plus all costs of manufacturing, processing, handling, sale, and delivery, including overhead costs.

Costs as applied to retail stores means invoice or replacement cost, whichever is lower, plus the cost of doing business.

Evidence of cost, based on impartial surveys or audits, made within a reasonable time prior to the alleged violation, shall constitute prima facie evidence of such cost at the time of such violation.

Rules and Regulations issued by the California Director of Agriculture specify in considerable detail what are and what are not acceptable cost accounting procedures. Further details are given in the Department’s Manual of Auditing and Costing Procedure for Processing and Distribution of Dairy Products.
prima facie evidence of a violation. On the other hand, regardless of costs, a retailer who sells for not less than 15 percent over the supplier's list price (or delivered invoice price or replacement cost) is presumed to be charging a lawful price. Similarly, wholesale vendors or sub-jobbers supplying retailers must sell at not less than a two percent markup over the prices paid.

Aside from routine checking and informal conferences the enforcement procedure under the Minnesota Law is about as follows:

1. When an alleged violation is called to his attention, the Commissioner serves the person or firm involved with a complaint, with a notice of hearing to be held in not less than 20 days. At such hearing the party involved is given an opportunity to show cause why an order to cease and desist from the practice complained of should not be issued.

Any person (including an aggrieved competitor) who offers a good reason may be permitted to intervene in the proceedings.

2. If the Commissioner finds as a result of the hearing and his investigations that a violation has occurred, he shall issue an order to cease and desist effective immediately.

3. The person ordered to cease and desist may apply for a review of his case by a state district court. When this is done, the Commissioner is required to certify the entire record of the case to the court.

4. If the court finds the Commissioner's order to have been justified, a court order commanding obedience with the law is issued. Violation of such an order, or of a cease and desist order upheld by the court, is punishable as contempt.

Advantages and disadvantages of program prohibiting the sale of milk below the seller's cost with the privilege of meeting a lawful price of a competitor. If successfully enforced a regulation prohibiting each dealer from selling for less than his cost but permitting him to meet the lawful price of a competitor, as in the Minnesota Law, would afford protection against extreme cases of price cutting.1

1/ Another requirement of the Minnesota Law, that which requires retailers to mark up the milk and specified milk products at least 8 percent, also may help to prevent the initiation of destructive price cutting in some instances.
On the other hand, this type of regulation would not prevent price wars of the chronic type (i.e., low prices over extended periods) during which a number of distributors, including some efficient ones, might be forced to operate at a loss. Moreover, unless combined with other provisions, as in the Minnesota Law, the prohibition of sales below the seller's costs with the privilege of meeting competition would provide only limited protection against unwarranted price discrimination. Consequently, this type of program meets only in part the Committee's requirements that to be acceptable a regulatory plan should be effective in meeting problems of destructive competition.

A significant advantage of this type of regulation as compared with the fixing of minimum resale prices is that the price-making function would be retained to a large degree in the hands of competing distributors. In theory, it would facilitate innovations and the development of low-cost distribution systems.1/

In some respects, the no-sale-below-cost type of regulation as prescribed in Minnesota, should be much easier and less expensive to enforce than the fixing of minimum resale prices. Since all dealers are in effect permitted to sell at the lowest prices established by an operator covering his costs, there will usually not be much pressure to undercut these lawful prices. Thus the extent of non-compliance and the risk of inequitable treatment of dealers subject to the regulation should be much less than it is when minimum resale prices are fixed. Moreover, the attention of the administrators can be focused mostly upon those dealers who file and charge the lowest prices. Ordinarily it will be necessary to analyze costs only for those who file and sell at the lowest prices.

As with other programs that involve regulatory control at the wholesale level, the administrative agency responsible for enforcing the no-sales-below-cost regulation would have the difficult problem of ascertaining indirect price concessions that may be given by a handler to effect a sale for less than the required minimum price.

The determination of unit costs for individual firms that are alleged to be selling illegally is sure to involve differences of opinion which in turn lead to controversy and to litigation. Among other things, the difficult question is encountered as to what cost basis to use in the case of a new distribution method or system where meaningful costs and potential economies can be determined only after a period of development.

Another disadvantage of this type of program is that minimum allowable prices are not definitely known in advance, as they are where minimum resale prices are fixed.

1/ Although the required filing of price schedules 10 days before they become effective, and other incidental aspects of the Minnesota system of regulation, may discourage competitive effort too much in some instances, this form of regulation appears likely to impose relatively little restraint upon the adoption of more economical methods of distribution as compared with a comprehensive price-fixing program.
Further difficulties arise in determining whether a price lower than cost has been charged or offered in good faith to meet the lawful price of a competitor. Is a distributor or group of stores on the other side of town or in another part of a large city a competitor? Can it be determined satisfactorily which of several competitors in an area struck the first blow in lowering prices in a retaliatory price cutting situation? Such difficulties are not insurmountable but they must be considered in judging the acceptability of such a program.

In summary, a program prohibiting the sale of milk below the seller's cost with the privilege of meeting a lawful price of any competitor would meet only in part the first criterion adopted by the Committee, namely the requirement that a given program be effective in meeting the problem of destructive competition. Moreover, the Committee fears that such a program might be so administered that it would interfere with the adoption of new methods of distribution and other innovations. Thus, it would only partially satisfy the second criterion of an acceptable program adopted by the Committee (page 36).

Prohibiting the Sale of Milk Below a Stipulated Floor Price at Retail

Instead of prohibiting the sale of milk below cost, with the privilege of meeting the lawful price of a competitor, a regulatory program designed to curb destructive price cutting might call for the fixing of a floor price below which no dealer would be allowed to sell. Alternatively, and with similar effect, such a program might require a specified minimum margin or mark-up over the dealers' buying price for fluid milk (Class I) as determined by a federal or state order.

This type of regulation was provided for in a bill that received serious consideration by the Connecticut Legislature in 1961.1/ It was also offered by an Advisory Committee of Economists for consideration in a revised system of regulating competition among milk dealers in New Jersey.2/

The Connecticut Minimum Margin Bill. The Connecticut bill, which had strong industry support but did not become law, would have authorized the Commissioner of Agriculture to issue and amend orders fixing the minimum marketing margins to be charged by dealers for fluid milk products over and above the

Class I price. Such action was to be contingent upon a finding by the Commissioner, on the basis of evidence received at a hearing, that emergency price stabilization was necessary because of one or more of the following conditions:

1. That a failure of dealers to pay producers in full on regular dates is threatened.

2. That substantial quantities of milk are being marketed by one or more handlers at a loss that is compensated for by profits from other products or services, or by drawing upon other resources; with the result that operations of small or independent milk marketing concerns are threatened, tending to injure competition and to create a monopoly.

3. That the regular, continuous and adequate supply of fresh milk from approved sources to meet normal requirements and protect the public health cannot be assured.

It is apparent that while the proposed law called for the fixing of minimum margins over the Class I price (i.e., the dealers' buying price for fluid milk established by a federal milk order), in effect this would be the same as floor price at retail or wholesale.

Under the proposed law, an order fixing the minimum marketing margin(s) would be limited to six months and the Commissioner would have no authority to extend it. No hearing could be held on a proposed new order until after the currently effective order had expired. The Commissioner could suspend or terminate an order after a public hearing upon finding that it tended to obstruct the declared policy.

The criteria set forth in the proposed Connecticut law required that the minimum margins:

1/ Under the proposed law, the Commissioner would have been authorized to fix minimum marketing margins for fluid milk, cream fresh or sour, skimmed milk, buttermilk, and flavored milk drinks. It is understood, however, that persons closely identified with the proposal favored the fixing of a minimum margin for fluid whole milk only.

2/ Had the proposed Connecticut legislation been adopted, it is probable that item 2 would have become the most important consideration for issuing orders to fix minimum marketing margins.
1. Be most in the public interest.

2. Best promote the milk industry of the state.

3. Assure a fair return to efficient milk dealers and retailers (the Commissioner would be required to consider "reasonable average operating expense, and reasonable return to the dealer in relation to the costs of processing and distribution").

4. Reflect economic conditions of supply and demand and normal trade practices in the area.

5. Effectuate the declared policy.

A further provision was that the minimum margin fixed by the Commissioner for milk should in no event be greater than the average of minimum margins for milk sold in gallon jugs at stores in all cities of the United States for which the essential quotations are published each month in the Fluid Milk and Cream Report, less two cents a quart. It is evident that this limitation might be in conflict with some of the foregoing criteria, particularly No. 3 and No. 4, and perhaps constitute a basis for litigation.

The minimum margins fixed by an order of the Commissioner would not apply to milk sold to schools, hospitals, or any state or federal agency.

The New Jersey proposal. The Advisory Committee of Economists which reported recently to the Secretary of Agriculture of New Jersey recommended an interim or transitional program which involved continued fixing of minimum retail and wholesale prices at "key points". They were unable to agree upon a long-run program of regulation but two members of the Committee favored the fixing of a single minimum marketing margin for milk sold to consumers. Again this minimum margin was to be a specified markup over the Class I price (i.e., the dealers' buying price for fluid milk, established by a federal order). It would amount to the fixing of a floor price at retail below which dealers or stores would not be allowed to sell. As explained in the Committee report1/ "the (floor) price in each area would include the raw product cost plus a marketing margin equal to the marketing costs of the most efficient way milk could be distributed...", presumably in gallon jugs through cash-carry dairy stores.

It is further explained that: "prices would be established after public hearings and costs would include a return on investment. Only the price of fluid whole milk would be regulated. The control agency would be expected to supplement dealer testimony by the results of cost determinations."

The New Jersey Advisory Committee acknowledged that no state has had experience with fixing a single minimum margin below which milk could not be sold. However, it was asserted that this type of regulation would have the advantages of simplicity, ease of enforcement, and advance knowledge of distributors as to whether contemplated prices would be legal or illegal. It permits wide latitude in competition and encourages the development of low-cost, efficient milk distribution, but it still provides a floor below which run-away competitive prices would be prevented from spiraling downward to “unreasonably low levels”.

Advantages and disadvantages of floor price(s) or minimum margin(s). Like the prohibition of sales below the individual dealer’s cost, the fixing of a floor price or minimum margin (perhaps only for fluid milk at retail) would help to prevent extreme cases of price cutting. It would also have the advantage of leaving price determination largely to market forces. However, it would provide relatively little protection against low prices over extended periods, during which many distributors might be forced to operate at a loss.

This type of regulation also has several disadvantages. Since the minimum margin or floor price would apply directly to only one product and type of sale (probably milk sold in gallon jugs at dairy stores or supermarkets) there is doubt as to the degree of stability such a program might bring to the prices of other dairy products and other types of sale.

A serious weakness of the single-floor price regulation appears to be its limited effect in curbing price cutting where it has been most serious, i.e., in transactions between milk dealers and store operators. Some dealers have expressed the belief that if prices were stabilized at the retail level, destructive competition in wholesale trade would no longer be a serious problem. However, past experience with resale price fixing indicates that this type of regulation is more effective at the retail level than in the sale of milk to stores and other wholesale customers. Stability of retail prices obtained through regulation often has been accompanied by widespread evasion of minimum wholesale prices.

The fixing of a floor price or minimum margin would facilitate the adoption of technological improvements and new low-cost methods of distribution to a much greater extent than a program of comprehensive price fixing, but probably to a lesser degree than the prohibition of sales below individual dealer’s costs. Even though the administrative agency attempted to establish the floor price or minimum margin in accordance with the costs of the most economical systems and methods of distribution, it undoubtedly would meet strong pressures for a more generous policy. Administrators would face insistent demands that the floor price or minimum margin be set at a level sufficient to cover at least the average costs of dealers in the market. Any lowering of the floor price or margin to give low-cost innovators an opportunity to become established no doubt would be resisted vigorously.
From the standpoint of economy of administration and adequacy of enforcement, the fixing of a floor price or minimum margin, as outlined herein, would have significant advantages over either the fixing of minimum resale prices or the prohibition of sales below cost. Even so, there may be a serious question as to whether such a program offers the prospect of sufficient benefits to outweigh the administrative effort and expense involved.

Like the prohibition of sales below the individual dealer's cost, the fixing of a floor price or minimum margin would meet only in part the problem of destructive competition. Moreover, the Committee fears that such a program might be so administered that it would interfere with the adoption of new methods of distribution and other innovations. It would be even less likely to fully satisfy the second criterion of an acceptable program adopted by the Committee (page 36) than a program prohibiting sales below individual dealer's costs with the privilege of meeting the lawful price of a competitor.

Prohibiting Unwarranted Price Discrimination and Regulating Other Trade Practices

Practically all states that have undertaken to regulate retail and wholesale prices of milk also have attempted to regulate certain trade practices which might be used to circumvent the enforcement of the stipulated prices. A large number of other states also have enacted laws for the purpose of curbing practices considered by the legislatures involved to be unfair and destructive. Some of these laws pertain to business transactions generally, while others deal specifically with sale of milk and milk products.

The California Ban on Unfair Practices

The Agricultural Code of the State of California contains a very detailed set of regulations pertaining to trade practices. In addition to the practices which are listed in the law as being unfair and unlawful, the Director of Agriculture has promulgated rules on this subject. A condensed listing of practices banned by the State of California, with respect to the sale of milk, cream and dairy products by manufacturers, distributors, wholesalers and retailers, is as follows:

1. Payment or acceptance of secret rebates or unearned discounts on dairy products sold to a customer.

2. Sale of other merchandise to dairy product customers for less than regular prices, or granting of unusual discounts, rebates or allowances on such merchandise.
3. Gifts or payments of any kind for the purpose of obtaining or holding a customer.

4. Extension of credit to customers beyond a normal period (60 days limit to wholesale customers).

5. Loans to customers or guarantee of loans obtained by customers from other sources.

6. Allowances to wholesale customers (or payment on their behalf) for advertising, displays, erection of signs, etc., except within specified limitations.

7. Furnishing premiums that call for the return of any part of the container as proof of purchase.

8. Furnishing of equipment, especially refrigerated cabinets, to wholesale customers without adequate compensation (very detailed rules on this).

9. Furnishing services to customers without adequate compensation. (Especially mentioned are: Installation or repair of equipment, preparation of tax returns, taking of inventory, etc.)

10. Any arrangement, such as the purchase of property from customers for more than actual market value, or sale of property to customers at less than market value, which amounts, in effect, to a discount or rebate on dairy products purchased by the customer.

   Purchase and lease-back arrangements are prohibited.

11. Discrimination in prices charged wholesale customers or consumers for dairy products of like grade and for similar services, where the effect may be substantially to lessen competition or to injure or destroy or prevent competition with the person who either grants or knowingly receives the benefit of such discrimination.

   (But price differentials which make only due allowance for differences in cost of the raw products or in costs of manufacture, processing, sale or delivery, resulting from different methods or quantities, are permissible.)
12. Sale of milk, cream or dairy products at less than cost. Cost, as applied to manufacturers and distributors means the cost of raw product, plus all costs of manufacturing, processing, handling, sale, and delivery, including overhead costs.

Note: Notwithstanding the foregoing prohibition of sales below cost, a manufacturer or distributor of milk and dairy products is privileged to meet, in good faith, a lawful competitive price or a lawful competitive condition.

13. False statements by wholesale customers or consumers to distributors or manufacturers concerning prices or terms of sale offered by competing suppliers, for the purpose of obtaining dairy products at unlawful prices.

14. Any false or misleading advertising.

Additional requirement: 1/

All persons subject to these regulations must keep specified kinds of records and make them available to the Director.

It is evident that the main purpose of prohibiting most of these so-called unfair practices by Minnesota, California and other states is to reinforce the requirement that persons subject to the regulation sell milk and specified dairy products for no less than the stipulated minimum prices. (The prohibition of price discrimination may be an exception, however.) A possible alternative would be to deduct from the prices actually charged the amount or value of any discounts, rebates, allowances, gifts, or concessions of any kind, granted to the customer. Then, if the net price were found to be less than the stipulated minimum, it would constitute a violation.

1/ As previously mentioned, the Dairy Unfair Trade Practices Act of Minnesota also prohibits an extensive list of practices that are declared to be unfair. The Minnesota list practically duplicates the California list summarized above, but includes a few additional specifications. It prohibits distributors from paying for licenses required of retailers, payment for rental of space in retail establishments, furnishing of free coupons, stamps, and the like, and the sale of milk and other products at combined prices less than their aggregate price when sold separately.
Many So-called Unfair Practices Customary in the Industry

Many of the trade practices that are declared by the laws of various states to be unfair, tend to be a "natural way of life" among milk dealers. Prohibiting such practices as secret discounts, unusual credit arrangements, the furnishing of free equipment, advertising allowances, and the like would tend, both in the short run and in the long run, to lessen competition and to increase the possibility of monopolistic abuses. This was especially true of a proposal considered by the New York Legislature in 1963 which called for prohibiting the advertising of milk at a specified price by milk dealers or stores.

The fact is that many of the so-called unfair practices are accentuated when marketing margins are greater than necessary to cover the costs involved together with a normal return on the invested capital. This Committee does not believe it would be in the public interest to use the police power of the State to suppress such practices in New York State.

Price Discrimination

On the other hand, there is one type of unfair trade practice which, if allowed to be used without restraint, may result in weakening and ultimately eliminating many efficient milk dealers. That practice is price discrimination -- the sale of milk or milk products to various customers or in various sales areas at different prices, where such price disparities cannot be justified by differences in grade or quality, or differences in costs associated with quantities sold, size or type of container, or service performed. (See item 11 of the foregoing list of practices banned in California, page 50.) A seller is permitted, however, to meet the lawful price of a competitor.

The Committee is especially concerned about the possibility that dealers having operations diversified as to products, distribution channels, or markets may sell certain products, or in certain outlets, or in a particular market, at a loss which is compensated for by earnings in other segments of their business. This type of unfair practice may at times have the effect of substantially lessening competition and promoting a trend toward monopoly. It is a type of practice which can be used by large, diversified firms with very damaging effect upon more specialized and more localized competitors.

Acting under authority of the Robinson-Patman Act, the Federal Trade Commission has directed much effort toward the suppression of price discrimination in business transactions generally. It has issued many complaints against dairy firms for engaging in this practice, and has had enough success in its enforcement activity to create a considerable amount of respect for its authority. However, the jurisdiction of the Federal Trade Commission is limited to interstate commerce and its resources are too limited to permit it to undertake intensive campaigns against price discrimination in the sale of milk. It is able to deal with only a limited number of cases and violations may go on for many months before action can be taken to halt them. In the meantime, competitors suffer serious damage.
At present, New York State has no legislation which makes price discrimination unlawful. The State Milk Control Law makes no mention of it.

The Committee believes that legislation to ban unwarranted price discrimination in the sale of milk in New York State would be a significant step toward meeting the problem of destructive competition. Such legislation should, as the federal law and laws of other states provide, authorize civil suits by injured parties to recover damages resulting from illegal discrimination.

A ban on unwarranted price discrimination would meet the Committee’s second requirement for an acceptable regulatory program in that it would encourage adequate and effective competition and offer no obstacle to the adoption of improved practices and low-cost distribution methods.

From the standpoint of feasibility and economy of enforcement, a state ban on price discrimination would be preferable to the fixing of minimum retail and wholesale prices. This type of regulation probably would involve difficulties and expense similar to those involved in the prohibition of the sale of milk below cost of the lowest-cost distributor. To minimize enforcement problems and expense, and to be most effective, the regulatory agency should focus its attention on situations in which retail or wholesale prices of milk appear to have been driven to unreasonably low levels.

It would be especially desirable for the state enforcement agency to seek close cooperation with the Federal Trade Commission in dealing with cases of discrimination that involve interstate commerce.

The Fact-Finding and Educational Approach

The several forms of regulation heretofore described, for dealing with the problem of destructive competition in the sale of milk, call for prohibitions and penalties that give rise to serious difficulties of enforcement. Some regulatory programs also have the disadvantage that they tend to prevent or delay adjustments in milk distribution that would be beneficial and desirable. It is well to consider, therefore, whether the alternative remedy of fact-finding, education, publicity and moral suasion might be more desirable.

The Milk Control Laws of New York and other states authorize the regulatory agencies to conduct investigations, subpoena milk dealer accounts and records, hold hearings and the like, primarily as a means of obtaining evidence of violations. As stated previously, the New York law gives the Commissioner of Agriculture and Markets the right “to investigate all matters pertaining to the production, manufacture, storage, transportation, disposal, distribution and sale of milk and milk products in the state....” He may subpoena milk dealers and their records and any other persons from whom information may be desired to carry out the purpose and intent of the law.
The New York Law further provides that: “It shall be the duty of the Commissioner to examine and audit from time to time, ... the books and accounts of milk dealers and cooperatives licensed under this article, for the purpose of determining how payments to producers ... are computed ... and for the purpose of determining ... the manner of disposition of the total income of each and every milk dealer or cooperative ... The Commissioner may reveal any of the findings of such examination or audit ... or may publish all or any part of such findings as in his judgment will best serve the public interest and accomplish the purposes of this chapter.”

Under another section of the New York Milk Control Law the Commissioner is authorized to require milk dealers to keep records, which are listed comprehensively, and to file such reports as may be specified from time to time.

No doubt the principal purpose of conferring such authority on the Commissioner was to enable him to obtain evidence of violations of the law or of his orders. Another purpose may have been to enable the Commissioner to ascertain the need for additional or revised regulations. And, whether so intended by the New York lawmakers or not, the provision for such investigational processes undoubtedly has served on its own account, to a limited degree, as a deterrent to the use of unfair or destructive trade practices. If desired, this effect could be made a major objective of investigational activity rather than a minor one.

Should it be found desirable to adopt the fact-finding educational approach to dealing with unfair and destructive competition in the sale of milk in New York State, the Milk Control Law should be amended to this effect. The law should state clearly that the Commissioner is charged with the responsibility of leadership in the promotion of active and fair competition in the distribution of milk and with the discouragement of unfair or destructive trade practices, as well as with the responsibility for exposing and discouraging monopolistic abuses such as arbitrary enhancement of prices or charges, collusive agreements, and the like.

To this end the Commissioner should be especially authorized to investigate situations in which unfair and destructive practices or monopolistic tendencies harmful to the public interest are alleged to exist; also to conduct trade conferences, to hold public hearings, and to publish findings and recommendations on these matters. “Unfair and destructive practices harmful to the public interest” should be defined to include unwarranted discrimination in prices charged different customers or in different sales areas, the sale of milk at prices so low as to threaten the survival of efficient, low-cost competitors, and other practices likely to have the long-run effect of lessening competition or increasing the possibility of monopolistic abuses.

In order to carry out such responsibilities to the best advantage, the Commissioner would need to establish a strong foundation of factual information about the market structure; trade channels and methods of distribution; marketing agencies and their services; prevailing trade practices; prices paid and
charged by dealers, stores and other agencies; and costs of handling, processing, packaging and distribution in important markets of the state. In particular, he should be informed about the costs of efficiently operated, economical systems of distribution as a bench mark for judging what prices and charges are reasonable in the various markets and under differing circumstances.

If such a foundation were inadequate at the outset, as it appears to be in New York State presently, an intensive program of fact finding should be undertaken during the first two or three years to accumulate the basic information that is needed. This would call for a major effort consisting, among other things, of carefully planned, selective, cost investigations, making use of qualified economic consultants and experienced teams of cost analysts. These investigations should be designed to reveal the range of costs for performing the essential marketing functions, and especially to indicate the possibilities of cost reduction, rather than to determine average or typical costs in the industry.

The program of cost finding sponsored by the New Jersey Department of Agriculture in 1963, though not endorsed in toto by this Committee, is a good example of the kind of undertaking the Committee has in mind. That program involved:

First, the development of a carefully drawn plan of investigation by an Advisory Committee of Economists.

Second, the selection, on recommendation of the Advisory Committee, of a firm of management engineers with much experience in this type of work to carry out the investigation as planned.

Third, the collection and analysis of cost data and related information pertaining to the handling, processing and distribution of milk.

A broad survey and screening procedure was used to obtain a general knowledge of operating conditions in the industry and to provide a basis for selecting a limited number of efficient low-cost operations for intensive study. In this activity the management engineers collaborated with the Advisory Committee.

Fourth, prompt publication of the findings of these investigations.

The Committee believes that carefully chosen economic consultants could be especially useful in connection with the planning of investigations, selection of qualified firms or agencies to perform contract services, analysis of the data collected, and preparation of the findings for publication.
The increased fact-finding activity that has been suggested for New York State would involve additional costs of administration, especially during the initial period while the basic cost data and pricing information are being collected and analyzed. On the basis of information pertaining to expenditures for somewhat similar programs, the Committee estimates that an annual budget of $200,000 to $250,000 may be needed for the initial fact-finding program covering a period of three years. The higher amount would be equivalent to about 1/4 cent per 100 pounds of milk received from farmers at New York State dairy plants. After the initial period of intensive investigation it should be possible to keep the essential information up to date and communicate it effectively to the industry and the public with an annual expenditure of about $150,000 a year, equivalent to less than 1/6 cent per 100 pounds of milk.

The task of developing and carrying out such a fact-finding and educational program would require the addition of several well-trained professional persons to the staff of the Division of Milk Control. The program might well be carried out in collaboration with appropriate research and educational institutions.

So far as known to this Committee, no state has adopted the fact-finding and educational approach as a major program for dealing with unfair or destructive competition in the sale of milk, although many states, including New York, have used it as a minor method of control. Obviously, fact-finding and educational efforts through conferences, hearings, publicity and the like would be a moderate approach to the control of destructive price cutting and other unfair practices. The Committee believes, however, that over time much could be accomplished by this method to lessen the problem of destructive competition.

The fact-finding educational method meets fully our second criterion for an acceptable program in that it would involve no significant restraint upon the adoption of improved practices and low-cost methods of distribution.

From the standpoint of the feasibility and economy of satisfactory administration, the fact-finding educational method is clearly preferable to all others. The indicated budgetary needs for a fact-finding educational program are small in comparison with the cost of other regulatory programs that have been discussed. Moreover, the money spent for fact finding and education would be used constructively, to improve the functioning of the competitive system and to bring about more efficient performance of marketing services, rather than for a purely regulatory purpose.
Part III

Summary and Recommendations

Summary

In the foregoing sections of this report, problems relating to both destructive competition and to inadequate or ineffective competition in milk distribution, as well as problems relating to present regulatory programs, have been discussed. Although some of these problems are serious and call for remedial action, the Committee believes that the milk distribution system in New York State and the regulatory program pertaining to it on the whole are functioning in the public interest. Milk of generally high quality is reaching consumers in ample quantities through a variety of distribution channels and outlets.

Technological innovation in milk processing and distribution, though restrained somewhat by industry discipline and through restrictive licensing of milk dealers by the State, has made substantial progress. Many dealers have adjusted their operations to changing conditions and have improved the efficiency with which they perform the essential marketing services. Milk distributors apparently are not making abnormally large profits.

Sporadic outbreaks of destructive price cutting, often associated with the introduction and development of specialized, low-cost, limited-service systems of distribution, have caused turmoil and distress in some segments of the trade. To date, however, there is no clear evidence of impending loss of essential marketing services or domination of the market by powerful firms or interests.

Producers in the State are being paid regularly, mostly in accordance with the terms of federal and state milk marketing orders.

Thus the Committee conceived its task to be one of devising and recommending measures that would help to make the present competitive system of milk distribution even more efficient and serviceable, rather than one of making proposals to reorganize the system extensively. It was also conceived to be the Committee’s function to suggest desirable changes in the State’s regulatory program pertaining to the sale of milk—changes designed to assure continuing and perhaps more rapid progress toward improved efficiency in the performance of services needed by producers and consumers.

Factors Causing Unstable Prices and Destructive Competition

Several attributes of the business of processing and distributing milk make it unusually susceptible to intense price competition, occasional price wars and various unfair and destructive practices. These attributes include:
1. The existence of excess capacity of plants and distribution facilities coupled with relatively low costs of serving additional customers and handling additional volume. This condition constitutes a strong incentive to seek additional sales by making price concessions to new customers.

2. The rapid adoption of new technology and methods of distribution resulting in lower costs.

3. The nearly universal use of milk and its importance in the consumer’s food budget; also the fact that consumers purchase milk more frequently than most other foods. In consequence, many consumers tend to be especially “price conscious” with respect to milk, and store operators consider milk a good “traffic builder”.

4. The relatively small brand preference for milk among consumers, which means that many housewives tend to seek the lowest available price without regard to the brand name.

In recent years, the rapid pace of technological changes and innovations in the transportation, processing and distribution of milk has been a particularly important factor tending to disrupt established marketing arrangements and price structures. The major innovations and changes taking place include:

1. The increasing importance of milk distribution through stores and the corresponding decline of home delivery.

2. The use of light-weight paper containers in place of glass bottles and the use of multiple-quart containers in place of single quarts.

3. The replacement of numerous small food stores by large, self-service supermarkets, many operated by chain merchandisers. Some of these have pushed the sale of milk aggressively.

4. The development of specialized milk delivery operations to serve groups of supermarkets on a volume basis at low costs. In some cases this involves the entry of food store chains into the operation of milk pasteurizing plants and delivery operations.
5. The increasing number and importance of specialized dairy stores, many of them operated by aggressive chain merchandisers.

6. The increasing importance of institutional outlets for milk, such as schools and military establishments.

7. The development of fast super highways and mechanically refrigerated trucks; these, together with the increased use of paper containers, the increased importance of large food stores as outlets for milk and increased economies of scale in processing, have brought a marked expansion of the areas served by many pasteurizing plants.

Steadily rising labor costs have stimulated many milk dealers to take advantage of new technology and opportunities for revised methods of distribution in order to lessen the impact of the high labor rates upon their unit costs.

**Impacts of Changes in Distribution and Price Wars**

These developments, together with the other characteristics of the industry mentioned previously, have led to outbreaks of intense price competition and retaliatory price cutting, sometimes driving prices and margins so low as to cause serious hardship for many milk dealers and their employees. On the other hand, in the short run at least, consumers and most producers appear to have benefited from these developments.

In recent years, the development of specialized, limited-service distribution systems, especially dairy stores, has resulted in particularly keen price competition in certain markets. The Committee believes, however, that the benefits of these specialized, low-cost systems of distribution outweigh any disadvantages from the viewpoint of the public interest. Therefore it concludes that such systems should be allowed to develop without regulatory interference except as to the prevention of unwarranted price discrimination.

The process of adjustment to changing conditions, painful as it is to many, is likely to continue regardless of what is done in the way of regulatory action. Most of these hardships are inescapable in a competitive system. Competition in pricing as well as in marketing services is an essential part of the competitive system under which the major part of the economy operates. It provides the stimulus for increased efficiency and for the adoption of improved, more economical methods of distribution to the ultimate benefit of consumers, producers and many of the marketing agencies.
Nevertheless, the Committee is concerned about the continuation of destructive practices in the industry that develop in the competitive environment that now exists in New York State. The most serious of these competitive abuses are the sale of milk at unreasonably low prices (which the Committee defines as prices so low as to make the position of efficient, low-cost competitors untenable) and unwarranted price discrimination in the sale of milk to different customers or in different sales areas. Such abuses run counter to accepted principles of equality of opportunity. They may involve the exploitation of inequality of bargaining power and of economic strength without regard to efficiency.

It is possible that in the long run consumers and producers as well as many dealers may be harmed through the impairment of the market structure so that the competitive vitality of the industry is reduced or useful distribution services such as home delivery are eliminated. Unfortunately, the danger that unrestricted competition will lead to such harmful results is difficult to assess. This risk, however, should not be ignored.

**Difficulty of Distinguishing Between Fair Competition and Destructive Competition**

It is difficult to distinguish between competition that is really destructive in the sense that it is potentially harmful to the public interest, and that which is beneficial to that interest, even though it may be distasteful or injurious to firms that cannot compete successfully. This is true especially in a time like the present when consumers' preferences for the various products, packages and methods of distribution are changing rapidly and when new technologies and distribution methods are having a pronounced impact upon marketing costs and the size of business required to achieve low unit costs. Because the distinction between desirable and undesirable forms or degrees of competition is difficult, exceptional care should be taken lest regulatory actions interfere too much with desirable forms of competition.

**Possible Need for Additional Regulation**

New York State, unlike many others, presently has no regulation of retail or wholesale prices of milk and comparatively little regulatory control over trade practices in milk distribution. In accordance with the foregoing analysis, it would seem desirable for the State to have the authority to curb the most serious abuses if there were reasonable assurance that the exercise of such authority would do more good than harm. Whether by some appropriate extension of regulatory procedures, competitive abuses could be minimized without losing the important benefits of competition--primarily the benefits associated with the essentially unhindered adjustments toward more economical distribution methods and systems--is the main question to which this report is addressed.

Appraisal of Various Kinds of Regulatory Programs

In evaluating the desirability of the various kinds of regulation that have been proposed or considered for the control of destructive price cutting and other unfair practices in the sale of milk, the Committee used the following criteria:

First, the extent to which a given program would meet the problem of destructive competition and its probable effectiveness for that purpose.

Second, the extent to which such a program would facilitate adequate and effective competition and prompt adoption of more efficient practices and low-cost methods of distribution.

Third, the feasibility of satisfactory administration and enforcement at reasonable cost.

Each of the various kinds of regulatory programs analyzed by the Committee has been evaluated in accordance with these criteria.

Fixing minimum resale prices of milk. One type of remedy for the problem of destructive competition in the sale of milk that has been used in many states since 1933 including (at one time) New York State, is the fixing of minimum retail and wholesale prices of milk and fluid milk products. During recent sessions, the New York State Legislature has passed bills that would have authorized regulatory programs which represent modifications of traditional resale price-fixing programs. A bill passed in 1961, but vetoed by the Governor, provided for emergency price-fixing authority. A bill passed in 1963, and likewise vetoed by the Governor, called for prohibiting the sale of milk at prices below the average costs of firms operating in a particular market.

The Committee finds that this type of regulation, together with its various modifications, would not provide a satisfactory solution to the present problem. It fails to meet the three stated requirements of an acceptable program. Price fixing has not been satisfactory in the past. Such regulation seriously interferes with adjustments that are desirable from the viewpoint of producers and consumers. Moreover, experience has shown such a program usually involves great difficulties of enforcement.

Prohibiting sales at unreasonably low prices. The laws of various states pertaining to regulation of resale prices and trade practices of milk dealers reveal different concepts as to what constitutes “unreasonably low prices.” Some states have adopted the prevailing price in a market or the average costs of representative dealers in a market as the test of reasonableness and legality. Others, such as Minnesota, permit each dealer to sell at his cost with the privilege of meeting a legitimate price of any competitor. The latter type of regulation avoids the rigidities inherent in the fixing of minimum resale prices and
leaves the determination of prices largely to the forces of competition. Theoretically, such a program would involve relatively little interference with desirable forms of competition; would present no obstacles to the introduction of more efficient, more economical methods or systems of distribution; and would not seriously delay the elimination of inefficient methods or firms. If satisfactorily enforced, this type of regulation would help to contain the more drastic cases of price cutting by providing a minimum floor under prices. It would not prevent, however, low prices over extended periods, during which many distributors, including some efficient ones, might be forced to operate at a loss. Moreover, unless combined with other provisions, this type of regulation would offer only limited protection against unwarranted price discrimination. Thus, it would meet only in part the problem of destructive competition.

A regulatory program that fixed a single floor price or minimum marketing margin could be administered relatively economically and effectively. Prohibiting sales below the seller's cost with the privilege of meeting a lawful price of a competitor would involve more difficult administrative problems than the fixing of a single floor price. Both types of regulation would involve difficulties in determining meaningful costs for new methods of distribution. In either case, but particularly where a floor price or minimum margin is fixed, the control agency probably would be subject to strong pressure to use its authority to maintain prices at higher levels than necessary to cover the costs of the more efficient firms and to exercise its power to harass and intimidate potential innovators and aggressive competitors.

On the basis of these considerations, the Committee concluded that there was not sufficient assurance of net gains to society from prohibiting sales at unreasonably low prices to justify the adoption of such a program.

Prohibiting unwarranted price discrimination. Of all so-called unfair trade practices that exist in the distribution of milk, the Committee believes that the sale of milk by a dealer to certain customers at lower prices than to others, or in certain areas at lower prices than in other areas, without adequate justification by differences in costs, is the one likely to be most serious from the viewpoint of the public interest.

The Committee is especially concerned about the possibility that dealers having operations diversified as to products, distribution channels, or markets may sell milk in certain outlets or in a particular market, at a loss which is compensated for by earnings on sales in other markets or outlets. This type of unfair practice may, and probably does at times, have the effect of substantially lessening competition and promoting a trend toward monopoly. It is a type of practice which can be used by large, diversified firms with very damaging effects upon more specialized firms and those whose operations are confined to a single market.

Legislation prohibiting unjustified price discrimination within the State would meet to an important degree the first of the three criteria established by
the Committee to test the acceptability of regulatory programs designed to curb destructive competition. If properly administered, such a program also would meet the Committee's second requirement by facilitating adequate and effective competition and offering no obstacle to the adoption of improved practices and low-cost distribution methods. By no means, however, should the proposed ban on discriminatory pricing be interpreted as requiring price uniformity without regard to differences in quality of product, quantities sold, services performed or other conditions which give rise to significant differences in costs.

It is recognized that a state regulatory program designed to prevent unwarranted price discrimination among customers and markets would involve difficult enforcement problems. One of these is the difficulty of determining the differences in costs incurred by a dealer in servicing customers who are charged different prices, as well as the differences in costs involved in the distribution of milk by a given dealer in different marketing areas to which different price schedules apply. In many instances, consideration would have to be given to subtle differences in products and services and many of the comparative cost determinations would involve cost budgeting as well as the analysis of cost experience.

Another set of difficulties would arise in attempting to determine in various instances whether a lower price charged by a given dealer to certain customers or in certain areas was made in good faith to meet a lawful price charged by a competitor.

However, the Federal Trade Commission has been moderately successful in the enforcement of such regulations, with respect to interstate commerce. The Committee believes that worthwhile results could be obtained through such legislation in New York State if the enforcement effort were concentrated upon situations in which discriminatory pricing appears to be associated with price cutting that has driven milk prices to unreasonably low levels. It would be especially desirable that the state enforcement agency, presumably the Department of Agriculture and Markets, collaborate closely with the Federal Trade Commission in policing the proposed ban on unwarranted price discrimination.

Prohibiting other trade practices. Several states have laws and regulations prohibiting specified trade practices such as secret discounts and rebates, tie-in sales, provision of free goods or services, advertising allowances and the like. In states where minimum resale prices are fixed, such trade practices are banned in an effort to prevent circumvention of the minimum price orders. In other states, the prohibition of a wide range of so-called unfair practices is a major regulatory program.

Many of these practices tend to be customary among milk dealers and other business groups. Past experience indicates considerable difficulty in enforcing regulations that prohibit such practices. There is also a danger that a regulatory program of this nature would tend to inhibit competition and encourage monopolistic abuses. Moreover, the Committee believes that if unwarranted price discrimination were effectively prohibited, other so-called unfair trade practices would be of little consequence or concern.
Fact-finding and education. In addition to the several types of regulation that involve prohibitions and penalties, the Committee has considered a program of fact-finding and education as a possible remedy for unfair competition in the sale of milk.

The Commissioner of Agriculture and Markets already has broad powers under the Milk Control Law to investigate all phases of the milk industry. It is evident that under present law this authority is intended to be used primarily as a means of obtaining evidence of violations of the law or of the Commissioner's orders. The Committee believes, however, that fact-finding through investigations, hearings and the like, coupled with educational efforts through conferences and publicity, should be adopted as a major program for raising standards of competition in the milk industry.

This would involve a change in the Milk Control Law to give the Commissioner a clear mandate to exercise leadership for encouraging active and fair competition among milk distributors and discouraging unfair and destructive trade practices through fact-finding and educational procedures. It would also involve providing additional funds to enable the Commissioner to undertake this added responsibility.

Fact-finding and educational efforts through conferences, hearings, publicity and the like would be a moderate approach to the control of destructive price cutting and other destructive practices. The Committee believes, however, that over time much could be accomplished by this method. A fact-finding and educational program would meet fully the second criterion for an acceptable program in that it would involve no significant restraint upon the adoption of improved practices and low-cost methods of distribution, in fact it could give positive encouragement to such desirable developments. From the standpoint of the feasibility and economy of satisfactory administration, this type of program is clearly preferable to all others.

An over-all appraisal. The Committee finds that none of the several forms of regulation which have been adopted for the purpose of stabilizing the resale price of milk or eliminating trade practices in milk distribution considered to be unfair and destructive has given a high degree of satisfaction. In many instances such measures have given rise to intense controversy and to a great deal of litigation. Moreover, they have not provided an environment conducive to the maintenance and expansion of the market for fluid milk and one in which this industry could continue to meet successfully the increasing competition of low-cost substitutes. There appears to be no state in which the benefits of such regulations have clearly outweighed the harmful side effects and costs involved.

The unfair and destructive trade practices that exist in this industry, however, are a matter of public concern. The Committee concludes that a fact-finding and educational program, coupled with the prohibition of unwarranted price discrimination, offers the greatest promise of dealing with the problem effectively from the viewpoint of the public interest.
Prevention of Monopolistic Abuses

The problem of destructive competition among milk dealers, which has commanded much attention in recent years and which is the focal point of this report, should not be permitted to obscure the indications of monopolistic practices that have appeared in this industry.

One of the general powers granted to the Commissioner in Article 2 of the Agriculture and Markets Law is the power “to investigate restraints of trade or unlawful combinations to fix prices.” The Committee believes, however, that the Milk Control Law (Article 21) should be amended specifically to charge the Commissioner with the responsibility of investigating in collaboration with the Attorney General of New York State, any evidences of unlawful restraints of trade and other monopolistic abuses that come to his attention.

Recommendations

From its analysis of the problems of competition and its evaluation of possible solutions for these problems, the Committee offers the following recommendations:

1. That no action be taken to authorize the fixing of minimum retail or wholesale prices of milk, either on a full-scale or on a limited basis.

The Committee believes that efforts to stabilize resale prices of milk through direct regulatory action would do more harm than good from the viewpoint of the public interest.

2. That the New York Milk Control Law be amended specifically to charge the Commissioner of Agriculture and Markets with the responsibility of using his influence through fact-finding and educational procedures to encourage fair and active competition in the milk distribution industry and to discourage unfair or destructive practices that tend to have the long-run effect of lessening competition and increasing the possibility of monopolistic abuses.

In his fact-finding and educational efforts the Commissioner should give special attention to situations that involve unwarranted discrimination in prices charged different customers in the same area or in different sales areas, the sale of milk at unreasonably low prices, and other practices likely to have the long-run effect of impairing the market structure, lessening competition, and thereby increasing the possibility of monopolistic abuses.
To provide a foundation for carrying out such responsibilities to the best advantage, the Commissioner would need at the outset to conduct intensive studies of the costs of handling, processing and distributing milk with special emphasis on the costs and related factors pertaining to efficiently operated, economical systems of distribution. Fact-finding and education should include obtaining information concerning market structure, trade channels, methods of distribution, marketing agencies and their services, trade practices, prices paid and charged by dealers and other marketing agencies as well as the costs of handling, processing, packaging and distribution.

The Commissioner should be provided with adequate financing for a fact-finding and education program. The task of developing and carrying out such a program would require the addition of several well-trained professional persons to the Department's staff. In addition, the Commissioner should be authorized to employ special consultants and to collaborate with public and private agencies with expertise in the areas of investigation, to assist in planning and conducting the studies and in reporting the findings.

Fact-finding and educational efforts through conferences, hearings, publicity and the like would be a moderate approach to the control of destructive price cutting and other unfair practices. The Committee believes, however, that over time much can be accomplished to lessen the problem of destructive competition. In addition, findings of the proposed investigations would provide excellent information for further analyzing the problems of destructive competition and for devising other suitable remedies.

3. That legislation be adopted by the State of New York prohibiting discrimination in prices charged for milk and other dairy products sold by milk dealers and stores to different customers of the same class or in different sales areas, except to meet competition or as justified by differences in costs related to quality, quantities sold, transportation and other services performed, where the effect may be substantially to lessen competition or tend to increase the possibility of monopolistic abuses.

As explained previously, this type of regulation strikes at a practice which is generally agreed to be unfair and contrary to the public interest. In many instances, unwarranted price discrimination is believed to be an important factor contributing to destructive competition and price wars. If successfully enforced, a ban on price discrimination would help prevent prices from being driven down to unreasonably low levels. Few milk dealers will long continue the sale of milk at prices which do not yield a reasonable return, for the purpose of driving out competitors, unless their losses in the particular market are offset by profits on other parts of their businesses.
The Committee recognizes that this type of regulation will not be easy to enforce. There will be difficult problems in determining whether, in cases of alleged discrimination, the price differences are justified on the basis of costs. Moreover, where an alleged violator contends that he discriminated only to meet competition it may be difficult to determine who was the first to cut prices.

The difficulties of enforcement should be surmountable, however, if the control agencies are well equipped for the task and concentrate their attention upon the cases that appear to be potentially most harmful to the public interest. In carrying out this program, it would be especially desirable for the state agencies involved to collaborate closely with the Federal Trade Commission which enforces the federal ban on price discrimination in interstate commerce.

As is done in federal legislation and in the laws of other states, the law banning unwarranted price discrimination in New York should authorize civil suits for damages, by private litigants, in addition to penalties imposed by the regulatory agencies.

The Committee believes that efforts to curb so-called unfair practices, other than price discrimination, through direct regulatory action would likely do more harm than good from the viewpoint of the public interest.

4. That the New York State Milk Control Law be amended so as definitely to charge the Commissioner of Agriculture and Markets with the responsibility to investigate complaints or instances of monopolistic abuse and report his findings to the Attorney General.

The types of monopolistic abuses that are of principal concern include collusive action in establishing wholesale and retail prices of milk, in bidding on public contracts for the sale of milk, and in restricting the marketing services offered to customers.

The Committee recognizes that the Commissioner has, as one of his general powers, the power “to investigate restraints of trade or unlawful combinations to fix prices”. However, it believes that the amendment of Article 21 of the Agriculture and Markets Law to charge the Commissioner with responsibility for investigating complaints or instances of monopolistic abuses would strengthen the protection that is now provided against such abuses. The fact-finding program proposed by the Committee would lend important support to this recommendation for control of monopolistic abuses.

5. That the Department of Agriculture and Markets follow a policy of granting and extending licenses to properly qualified milk dealers that will encourage effective competition and facilitate the adoption of new technology and methods of distribution.
From the viewpoint of the public interest, the licensing of milk dealers accomplishes several useful purposes. It aids in insuring that dealers are responsible financially as well as in other respects, and facilitates the enforcement of regulations pertaining to producer payments, sanitary regulations, product standards, and the like. The trend of recent years toward a more liberal policy in granting and extending licenses is commendable and further liberalization is desirable.

Improvements in highways, technological developments in the industry, new methods in the assembly, processing and distribution of milk, and changing patterns of population are increasing the distances over which milk can be distributed economically. These developments offer continuing opportunities for increased marketing efficiencies to the ultimate benefit of producers and consumers as well as many marketing firms. They should be facilitated, not hindered, by the Department of Agriculture and Markets in the exercise of its licensing authority.
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