

**PUBLIC REGULATION OF  
COMPETITIVE PRACTICES**

**STUDIES IN PUBLIC POLICY  
TOWARD BUSINESS**

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# PUBLIC REGULATION OF COMPETITIVE PRACTICES



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## FOREWORD

**T**HIS volume, like the study of "Trade Associations: Their Economic Significance and Legal Status" which preceded it, is an outcome of a comprehensive investigation of the problems raised by governmental regulation of industrial and business enterprise in the United States. Such problems are ever-present in a society in which manufacture and trade have undergone and are undergoing such rapid development and change as is witnessed in this country. Both this development of industry and trade and some form of government policy toward them are inevitable, and the flexible adjustment of the one to the other is necessary for economic security and progress.

The problems here involved, while interrelated and fundamentally one, present three aspects which for convenience have been distinguished and treated separately in the Conference Board's investigation. There are, first, the problems raised by the business practices of enterprises, regardless of their size or internal organization, in relation to competitors, dealers and consumers. These are problems of general business regulation arising out of the competitive process, the freedom of which it is the fundamental intent of all governmental policy in this country to preserve. Second, there are the special problems presented by the cooperation of independent business organizations in common lines of activity. These are the problems of the legitimate scope of trade association, which have been of increasing public concern, and which, because of the current interest in them, were treated earlier in the Conference Board's study in the volume mentioned above. Third, there are the problems raised by the large scale organization of business or industry through the consolidation or combination of independent interests. This is the "trust" problem itself, familiarly so-called, which presents in many respects the most difficult of all the problems of governmental policy toward business organization.

The present volume deals with the first of these three aspects of the regulatory problem. Its subject is not only of timely interest, but in the larger view it forms the bridge between the consideration of business cooperation and that of industrial combination, for the problems of the regulation of trade association activity and of large-scale industry are intimately bound up with those of the regulation of the competitive process in general.

In this, as in other parts of the Conference Board's investigation of the problems of governmental regulation, the primary purpose has been to seek the elements of sound public policy in this complicated sphere, not through a purely critical or negative approach to the existing policy, but through an analysis of the economic background in which any policy must function, in this way affording a basis for independent judgment upon the soundness and adequacy of the prevailing law and policy. While every effort has been made to make the survey of the legal situation as exhaustive and exact as possible, the emphasis in all these studies is placed primarily upon the economic rather than the legal aspect of the problems dealt with.

This volume is the result of an investigation conducted by Mr. Myron W. Watkins and assistants, of the Conference Board's Research Staff, under the general supervision of the Staff Economic Council.

In the preparation of its publications, the National Industrial Conference Board avails itself of the experience and judgment of the business executives who compose its membership and of recognized authorities in special fields, in addition to the scientific knowledge and equipment of its Research Staff. The publications of the Board thus finally represent the result of scientific investigation and broad business experience, and the conclusions expressed therein are those of the Conference Board as a body.

In this study the Conference Board has greatly benefited by the critical suggestions of numerous business executives, economists and legal authorities especially conversant with the subject of which it treats. To all of these the Conference Board wishes to express its indebtedness. The Board is under special obligation to the members of its Advisory Com-

mittee on Anti-Trust Policy and Enforcement, whose close cooperation has been invaluable, viz.:

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# PUBLIC REGULATION OF COMPETITIVE PRACTICES

## INTRODUCTION

### §1. POINT OF VIEW AND METHOD OF THE INQUIRY

The object of the investigation of which this study is a part is to survey the results of the policy of regulating manufacturing industry and trade which has been pursued in the United States in recent times. To do this properly, and thereby provide a basis for a sound judgment upon public policy in this sphere, it is essential to consider the problem from several points of view. The point of view of consumers, interested in fair prices and honest dealing, the point of view of producers, interested in technical efficiency and reasonable rewards, the point of view of the lawyer and political scientist, interested in simple, definite rules and effective administration,—none of these can be ignored. To take a single angle of approach would greatly simplify the study, but would correspondingly detract from its value. It has not seemed feasible, either, to make separate studies from each of these several points of view. The complexity and essential difficulties of the different aspects of government regulation of trade cannot be adequately appreciated and the problem effectively dealt with by this method. Accordingly, the method of procedure herein followed will be to treat the particular aspect of the regulation of industry and commerce which is the subject of this volume as an outgrowth, in its numerous phases, of certain trade conditions, which will be described and analyzed as a basis for the discussion of the legal issues which have developed around them.

Preliminary to the detailed examination of the various directions in which the government regulatory power has in-

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terfered with the discretionary conduct of private business enterprise in the market, it will be well to trace in broad outline the general characteristics of the political economy under which production and consumption are carried on, and which, after all, so-called anti-trust policy touches only on the fringe.

The system by which trade and industry in the United States have been organized and conducted from the beginning of the national life is perhaps best described as the competitive system. Whatever view one may hold regarding the beneficence or the disadvantages of this system, however closely or remotely one may regard its connection with the economic expansion of the country, it is indisputable that an analytical study of the operation of the competitive system must be the starting point of any inquiry into the nature of a sound public policy in the regulation of trade. For the competitive ordering of economic affairs is a corollary of some of the most fundamental of the established institutions in modern society. The competitive industrial system has grown up in conformity with the evolution of social and religious and political ideas, habits, and usages which have all contributed in stamping men living in modern communities with a certain character, a certain outlook, a certain bias, if you will. Their attitude towards work, their notions of rights and duties, their loyalties and their detachments, their ambitions and their complacencies,—in short, what men are,—is in great measure a result of the system under which they have been living.

In consequence, the formulation of a public policy towards any particular aspect of human relationships, such as the economic process, cannot be undertaken in the abstract without disregarding, at some hazard, this vital interconnection between the human material to be dealt with and the existing ways of doing things. Traditions, usages, institutions—the social heritage—may of course be modified. But they are not like a cloak which men may put on and take off at will. They are the muscular tissues which make the bony skeleton of “human nature” into a living organism. To wholesome nourishment these tissues respond, and to the diseases of the flesh they are subject. But large-scale surgery is a perilous

expedient, whether upon the body politic or the human organism, and is undertaken by sane men only in the direst extremities.

## §2. STATEMENT OF THE PROBLEM

Beginning, then, with this competitive economic order which is found actually administering to the wants of men and as well providing an outlet for some more epicurean impulses, there are certain salient features and essential implications thereof which must at once be noted. The competitive industrial system is at bottom a mechanism providing for the distribution of productive resources of all kinds among the various alternative uses of which they are capable, according to the spontaneous adjustment of private interests.<sup>1</sup> It assumes that each individual is the best judge of his own interest. It assumes that when left free to pursue that interest, each will find employment for his means where they are most fruitful not only for himself but, at the same time, for others. That these assumptions are wholly justified, without any qualification, there are few who would now contend. But, on the whole, with all its offsets, this system of economic liberty does appear to provide a reasonable measure of material welfare and at the same time afford men such a degree of independence and responsibility as comports with common human dispositions. This is attested by the adherence of the overwhelming majority of citizens, expressed in votes, to the political framework and government policies which support the traditional economic system in its main outlines.

The competitive system involves, it is manifest, the grant of a wide discretion to individuals to enrich themselves by whatever methods they can. But that a wide latitude in the choice of pathways to gain may result in the discovery that there are numerous ways by which one may profit at the expense of others, rather than along with them, has long been

<sup>1</sup> It is frequently asserted, also, that a competitive system of industry tends to procure such a flow of products of varied sorts that their relative quantities and qualities approximate the maximum satisfaction of wants from the limited disposable resources. Whether this result will be realized, however, depends upon the validity of certain assumptions regarding the competitive process which on *a priori* grounds seem reasonable enough, but which its actual operation does not always bear out. Cf. Alfred Marshall, "Principles of Economics," 7th ed., 1916, pp. 462-476, 502.

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realized. As a consequence, not even under the roseate illusions of the eighteenth century political philosophy did the government of any modern state, save for a brief period in France during the Revolution, abandon all regulation of the conduct of economic affairs. It has always been recognized that some authoritative restraints must be imposed upon men, in trade no less than elsewhere, if their intercourse is not to degenerate into a hectic process of mutual frustration. The prohibition of force and fraud applies in every field of human relations and probably has been, on the whole, as rigorously upheld in the sphere of business as outside of it. Indeed, as will presently be shown, under the common law, as developed in the decisions of English and American courts, there have long existed special rules applying the general principle of protection against forceful or deceitful aggression to the peculiar exigencies of trade. The prohibition of conspiracies against public order and the common welfare, extending far back into the origins of the common law, has likewise had special application to the affairs of trade and testifies to a persistent skepticism of the policy of exclusive reliance upon self-direction.

It is evident, therefore, that this is no new problem which confronts those responsible for the formulation of a sound public policy toward the management of industry. It is but the continuation of an old problem. It is ever a question of whether and how far changed conditions—objective changes in the environment, changes in industrial technique, possibly human changes connected with education and migration—counsel a new adjustment of the balance between freedom and authority in regulating the conduct of economic affairs. Some readjustment of this balance seemed necessary in the United States towards the close of the last century. The increase of immigration, the disappearance of the frontier, the establishment of rapid transportation and communication, the growth of large-scale manufacture, the expansion of markets from local areas to a regional and national compass, all these had such profound and far-reaching effects upon the economic life of the people that some modification of the traditional public policy toward the regulation of trade appeared indispensable.

It cannot be gainsaid that serious abuses had grown up under the stress and strain of the transitional period through which American business was then passing. Secret rebating, local price wars, spying upon and molesting competitors' salesmen, underweighing, and deliberate bribing of customers' agents characterized to some extent the business methods prevailing in not a few industries. Occasionally in an effort to escape from these chaotic and degrading conditions competitors would suppress their enmity for a time. But when the competitive warfare ceased through price agreement or output limitation or division of territory, the exploitation of the consumers usually commenced. Such was the vortex into which the business community was plunged by the rapid growth of manufactures and the breakdown of local barriers to trade under the impetus of the deep-seated forces above described. The old, established doctrines of the common law were still applicable, of course. But the situation had gotten to a stage with which, evidently, the indirect measures and slow processes of the courts could not cope.

### §3. GOVERNMENT REGULATION AND ITS SEVERAL ASPECTS

The problem presented was of national scope and called essentially for national action. Constitutional provisions, in this connection, presented no immediate barrier; the "commerce clause" furnished ample authority for the exercise of broad powers by the Federal Government, if Congress deemed this expedient. And it did. The Interstate Commerce Act of 1887 and the Sherman Anti-Trust Act of 1890 reflected a wide-spread conviction that the control of trade and industry had gotten "out of hand." Both of these important pieces of legislation expressed a determination to revise public policy in such fashion that the subversion of public interests by the manipulation of private business should be made less inviting. The government was to exert more actively its authority for the protection of the general public and correspondingly to curb the prerogatives going with the management of private property. The legislation of 1887 was directed primarily to the regulation of the railroads, and that of 1890 primarily to the regulation of industrial and com-

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mercial enterprises. They differed vitally in the scope and manner of the extension of public authority, and the declaration of public policy which each embodied has in both instances been considerably modified by subsequent amendments and supplements. But it is no part of the purpose of this Introduction either to describe in detail the provisions of these fundamental laws or to enumerate and interpret the legislative and judicial modifications they have undergone. This has been done summarily for the Anti-Trust Act in Chapter II of the first study in this series,<sup>1</sup> and will be briefly recapitulated in the third chapter of this volume. Here it is sufficient to observe that the development of government regulation of business enterprise in the last forty years, and in particular the evolution of anti-trust policy, has continually been in the direction of strengthening the competitive economic order. It has aimed, not at the substitution of government control for competition, but at safeguarding and invigorating competitive forces to the end that manufacture and commerce may spontaneously regulate themselves in the public interest.

### (a) *Anti-trust Policy and Industrial Consolidation*

In surveying the scope and operation of this anti-trust policy there are several divisions under which one might treat its various applications. But there are three principal aspects which commend themselves for a study of this character, involving an economic appraisal of the effects of the law. The policy of the law may be studied in its relation to industrial consolidation, in its relation to trade cooperation, or in its relation to business practices.<sup>2</sup>

The first is undoubtedly the aspect of anti-trust policy which has received the most attention, both critically by professional writers, and casually by politicians and publicists. The interpretation and enforcement of the anti-trust laws on this side have aroused grave forebodings, sanguine hopes, and

<sup>1</sup> National Industrial Conference Board, "Trade Associations: Their Economic Significance and Legal Status," New York, 1925.

<sup>2</sup> But it must not be forgotten that all aspects are closely interrelated, anti-trust policy as a whole having the single dominating object of maintaining free and open competition in all branches of industry and in all markets, save such as may be specifically exempted from its purview.



warm controversies. Even now the issues have not all been resolved; but they are less acute than they were a generation ago. The changes in business usage with the accumulation of business experience, and the progressive modification or adaptation of the principles laid down in the Sherman Act have combined to shift the main interest from this field of application to the others.

*(b) Anti-trust Policy and Trade Cooperation*

The relation of the public policy embodied in the Sherman Act and supplementary legislation to cooperation in trade and industry is a subject latterly receiving increasing attention. With the ebbing of the tide of industrial combinations and mergers in the first decade of the century, so much of the energy of American business enterprise as was unable to express itself in the responsible administration of industrial or commercial ventures sought an outlet in the remodeling of the trade and market structure. This was almost necessarily a cooperative undertaking. For the "structure" of trade relationships, i. e., the general framework within which private firms establish themselves and within which the goods and counters of commerce are moved about is, after all, if we leave aside for the moment the bare skeleton of legal rules, only a bundle of habits and usages. These can seldom be consciously modified or moulded save by the collective action of a representative group subject to their sway. It requires the warm influence of a common fellowship to loosen customs made rigid by long practice or to germinate the seeds of a new order in trade relations. Vast and powerful combinations, working separately, have often found themselves impotent to introduce adaptive methods and devices or to change old ones.<sup>1</sup> Single-handed enterprise in this direction begets hostility by virtue merely of its single-handedness. But through cooperate efforts it was found that there were manifold ways

<sup>1</sup> Take, for example, the occasional vigorous sponsorship of commercial arbitration by a prominent concern in a given line of trade. Its zeal to replace the costly but established system of litigation in the settlement of commercial disputes by the more expeditious plan of arbitration is usually met with indifference, if not with suspicion, or active hostility. The growth of a relatively novel device, such as commercial arbitration, has to be nurtured by the joint support of a number of independent factors in the trade.

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to alter the technical and market environment of trade competition to mutual advantage. Usually, though not invariably, these ways led through improvements in the efficiency of industrial and commercial processes to greater business profits. For example, it was found that the exploitation of patents, the diversification of products, the assembly of credit information and data upon the course of trade, the methods of estimating production costs, all lent themselves to cooperative attack.

It is manifest, however, that this cooperation among trade competitors which has been such a salient feature of industrial evolution during the last two decades was bound to encounter the challenge of the same principles of public policy which had exerted a limiting influence upon the consolidation movement. Similar questions arose, but in a new guise. What liberty should be vouchsafed to voluntary associations of producers to regulate in unison the conditions and usages in their respective industries? How far might these autonomous bodies in each field of trade safely be permitted to go in the exercise of the privileges accorded them? It was to find an answer to questions such as these that the investigation leading to the Conference Board's report on "Trade Associations: Their Economic Significance and Legal Status," was undertaken. The conclusions there stated need not here be repeated.

### *(c) Anti-trust Policy and Business Practices*

The relation of federal anti-trust policy to the business practices, or methods of competition, employed by individual establishments remained until recent years obscure and undeveloped. It had, of course, long been recognized under the common law, as was pointed out above, that there must be limits to the discretion granted the responsible managers of business enterprises as to how best to advance each his special interest. Aside from the limitations which adhered generally to men's behavior outside of business as well as in it, certain private rights of action existed in favor of business competitors injured by the business practices of a rival in trade. But these were of restricted compass, as will presently be shown. On the whole, every business man was expected to

look out for himself. If he did not, and suffered damages, they were likely to remain unredressed.

Not only were there few business methods or policies employed in trade competition which were regarded as tortious, but the regulation of these matters formed no part of what is sometimes indefinitely called public law. Such injuries as might be inflicted in the struggle for trade were for the most part considered excusable, or at best but private wrongs. "Business is business" justified much. But experience gradually revealed that there were public as well as private interests at stake in respect to the business tactics used by independent trade competitors. It became clear that nefarious tactics might be used to stifle competition. The policies of trade competitors mould the market environment and, according to their character, bring about conditions favorable to honest and forthright competition or to the arbitrary and monopolistic control of the market. They do this by their influence upon the qualifications for survival in the trade. If the energy of business managers must be continually engaged in checkmating the insidious and unfair aggression of unscrupulous rivals, the value of the competitive process from the social point of view is impaired and its attractiveness to the participants themselves must likewise suffer. It becomes only a question of time before such competition will be ended, either by the collusion of the exhausted and exasperated rivals or by the supremacy of the most predatory.

In response to the growing recognition of this vital connection between the plane of competitive business conduct and the maintenance of a free and open market, Congress passed in 1914 the most important supplementary legislation to the anti-trust law of 1890. Whether the arrested development of the common law in the limitation of competitive practices might eventually have been corrected in the courts, as some contended, or whether the principal deterrent to the indirect regulation of the competitive conduct of independent business enterprises under the Sherman Act was only the skepticism or supineness of prosecuting authorities, as others asserted, it is no longer of moment to inquire. The Federal Trade Commission Act and the Clayton Act taken together met the criticism that anti-trust policy was inadequate on its

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preventive side. The administration of these laws in the decade since their enactment has quite naturally given rise to sharp controversies over both the detailed regulations which they authorize and the fundamental development of policy which they embody. A sufficient period has now elapsed to warrant a systematic and analytical review of this newer aspect of anti-trust policy and the formulation of a judgment upon its utility. This is the task which has been essayed in the present study.

### §4. PLAN OF THE PRESENT STUDY

The plan of treatment will be to review first the main features of the transformation which commercial organization and usage have recently undergone. This will provide the economic background for the subsequent analysis of specific competitive practices and the policy of the law in regard thereto. A second chapter will be devoted to the limitations placed upon competitive tactics by the common law and to an examination of the expediency and effectiveness of those limitations. This will be followed by still a third chapter, more or less introductory in nature, dealing with the development of federal regulation of the methods of competition. In this connection will be discussed several influences which, quite apart from the influence of the 1914 amendments of the anti-trust law, have tended to ameliorate the conditions, and raise the standards, of trade rivalry. These influences may be regarded as abetting the work of the federal administrative agencies in certain directions, and in so far they must be taken into account in judging of the need and assessing the achievements of federal regulation.

In Chapters IV, V, and VI the real substance of the regulation by government of the modes of market conduct pursued by private enterprises is treated. The division of the subject matter follows, roughly, a natural economic division between the price policies, the sales-promotion policies, and the trade relations policies, of a business concern. This classification has been chosen in preference to a technical legal division, which could lend little assistance to an economic analysis of the rules and doctrines which go to make

up current public policy regarding the conduct of trade. In brief, the effort will be rather to determine how certain branches of business practice are affected by government regulation, than to find how in detail certain legal rules and administrative rulings affect business practice. These three chapters will constitute the body of the present study. A final chapter will afford an opportunity for directing attention to the larger implications of all this authoritative regulation of business conduct, and for weighing its advantages and disadvantages in the light of the actual situation. This may lead to the formulation of some general conclusions regarding the soundness of existing anti-trust policy in its application to the control of competitive practices.

## CHAPTER I

### MODERN CHANGES IN METHODS OF MARKETING

#### §1. RELATION OF COMPETITIVE PRACTICES TO COMMERCIAL ORGANIZATION IN GENERAL

Competitive tactics, in the broadest sense, would cover every feature of the conduct of a business enterprise. The adoption by a manufacturer of the policy of restricting his operations to the production of a particular type of product is a method of doing business calculated, whether the event proves rightly or wrongly, to give him an advantage over competing concerns. Likewise, the establishment of a given system of wage payment and employee pensions is in one sense a method of competition. But these are not the types of business policy which one has primarily in mind in discussing the fairness and lawfulness of competitive practices. Such policies relate primarily to the scope of the given business enterprise and to its internal administration. They give rise but infrequently to questions of public policy, of public law, or of political economy. It is on the side of commercial affairs, in connection with distinctively commercial relations, that the conduct of a business enterprise touches most closely the ethics and economics and law of trade organization. A manufacturer's price policy, advertising policy, and methods of salesmanship are the crucial features of his business conduct from the point of view of public policy in regard to the organization of trade and industry. Commercial relations represent the contacts of a business unit with outside parties in the ordinary course of trade, and it is these which have latterly come within the purview of those government regulations known as the anti-trust laws.

Few of the competitive tactics which are the subject of administrative regulation, in fact, few competitive tactics of any description, are directed immediately against trade competitors. Dealings between competitors are rare. To the

extent that actual business transactions occur the parties cease to be competitors, strictly speaking. They become either bargainers or confederates. As bargainers they are subject to the general rules of the law of contract and sales. As confederates they are subject to the law of conspiracy, of which one aspect of the anti-trust laws, previously treated in a separate volume,<sup>1</sup> forms an important branch. But strictly as competitors their dealings are with a common group, those on the opposite side of the market, and it is indirectly through the character or quality of their dealings with this group that business methods of traders most incisively affect the competitive process. It is this feature of business practice, therefore, which brings the conduct of independent, private enterprises into relation with anti-trust policy.

It should be evident, consequently, that an understanding of the nature or characteristics of current commercial organization and the tendencies in its development is indispensable to a critical examination of the economic legitimacy of, and the legal attitude towards, specific methods of conducting trade. The nature of the means employed by private concerns directly to promote the sale of their products depends very largely upon the prevailing system of commercial organization, and cannot be judged apart therefrom. To be sure, the system of transferring goods from factories to ultimate consumers varies from industry to industry. There is no uniformity in this system, or course of trade, and, moreover, it varies from time to time. But it does not seem unreasonable to undertake to specify some of the more general or pervading changes which have occurred in recent times, even though they have by no means had a like influence in all lines.

## §2. THE TRADITIONAL, OR REGULAR, CHANNELS OF TRADE

A half century ago what is now known as the "regular" or "traditional" channel of trade was common in most branches of industry. It consisted, summarily, of the manufacturer, the broker, or selling agent, the jobber or wholesaler, the retailer, the consumer. Finished goods passed from the

<sup>1</sup>National Industrial Conference Board, "The Trade Associations: Their Economic Significance and Legal Status," New York, 1925.

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manufacturer in relatively large quantities, equivalent often to a season's entire output, to be gradually split up and distributed in successive stages in ever-dwindling volume (of individual transactions) until they reached the hands of ultimate consumers. The commanding figure, the pivotal position, in this whole series of distributive operations was that of the jobber. He it was, typically, who interpreted the demand. The quantity, quality, and style of products were determined by him and the goods were commonly made up at his risk. Not unusually they were labeled with his trade mark, and in any case it was his responsibility to keep on hand a sufficient supply to meet promptly the market demand, however widely that might fluctuate. Seldom were sales made, beyond the wholesale stage, of goods not "ready for delivery." Sales were ordinarily accomplished by inspection, rather than by specification or even by sample. Prices all along the line were independently negotiated in each transaction. Some exceptions to this generalization, so far as applicable to retail trade, might have been necessary. But even in that sphere the exceptions had not become the rule fifty years ago. The relative infrequency and consequent relative scale of individual transactions tended to make price negotiation a constant and inescapable feature of business management.<sup>1</sup>

The responsibility was thus thrown upon business men of all ranks in every branch of trade to protect their own interests by bargaining skill; and incapacity to do this was regarded as unfitting a man for trade. If one were "beaten in fair trade" there was scant sympathy for the victim and little or no reproof for the more astute party. And "fair trade" was synonymous with free trade, i. e., any dealings in a legally free and open market. If a buyer, having inspected the goods and higgled over the price, could not look out for himself in the bargain, it was felt that it ill became him to complain. If other sellers could not outwit buyers similarly, and so could not retain their position in the trade, they had only themselves to blame for their failure. For were not the same devices open to them?

<sup>1</sup> For a brief description of the development of American domestic trade organization, see V. S. Clark, "History of Manufactures in the United States, 1607-1860," Washington, 1916, pp. 354-360.



### §3. DISLOCATION OF THE ESTABLISHED SYSTEM OF TRADE ORGANIZATION

All this has been materially changed in most branches of trade during recent decades. The "regular channels of trade" have been disturbed and disfigured until only their outlines are still traceable here and there. The "merchant prince" of former days has been displaced by the "captain of industry," and the latter in turn is now challenged.<sup>1</sup> The jobber no longer dominates the entire productive and distributive process. In many fields he seems to be disappearing altogether.<sup>2</sup> His function of "interpreting the demand" has been transferred and transformed by the insistent urge of the manufacturer to "create a demand." The "regular retailer" has likewise suffered, and under the influence of much the same forces. His function of anticipating customers' wants and of representing them in the selection of unstandardized merchandise has been largely superseded.<sup>3</sup> The consumer does not require the services of a specialist in judging the

<sup>1</sup> Cf. Alfred Marshall, "Industry and Trade," London, 1919, pp. 171-174.

<sup>2</sup> In a series of studies made a few years ago by the Bureau of Foreign and Domestic Commerce, Department of Commerce, appeared the only readily available data from official sources bearing upon this transformation. The *Report upon the Knit Underwear Industry* (Miscellaneous Series No. 32, Washington, 1915, p. 39) disclosed that of the total volume of net sales of the 63 knit-goods establishments reporting, 55.45 per cent was made to jobbers. The *Report upon the Shirt and Collar Industries* (Miscellaneous Series No. 36, Washington, 1915, p. 29) showed that "of the total sales of the 42 establishments reporting, . . . 38.76 per cent was sold to jobbers." Other reports indicate even smaller percentages of the annual volume of trade as passing through the hands of jobbers; in the case of men's ready-to-wear clothing the amount handled by jobbers was less than 2 per cent of the total.

A passage in the *Report upon the Hosiery Industry* (Miscellaneous Series No. 31, Washington, 1915, p. 155) is most significant. "The branding of hosiery," it is explained, "has resulted in a material change in selling methods. Large manufacturers are gradually giving up selling to jobbers and are devoting their attention to selling to the retail trade exclusively. By selling to retailers they can advertise their own trade-marks, and the public can be benefited by being able to buy standardized products."

<sup>3</sup> The changes in consumers' buying habits since the advent of standardized merchandise have in many respects been startling. It would be interesting, though perhaps not so profitable, to undertake an intensive survey and analysis of this subject which has hitherto received but casual and incidental attention by agencies of commercial research. If shoppers no longer carry magnifying glasses to enable them to count threads in piece goods, does this indicate a growing trustworthiness of manufacturers and a better acquaintance with their brands? Or does it indicate the abandonment of an unnecessary suspicion of retail traders? Or does it reflect an increasing ignorance of merchandise values among consumers, with the disappearance of household crafts? Cf. White, "Market Analysis," New York, 1921, p. 129.

quality of goods which may be ordered by name, with their grade or formula plainly stamped upon them. Whether rightly or wrongly, the manufacturer's widely advertised representations regarding the composition of his identified product and claims for its quality are now accepted by buyers where the verbal assurances of dealers were formerly relied upon. Retail distributors in many lines, consequently, have been driven to seek patronage almost exclusively upon the basis of the price appeal. But for this purpose the rapid turnover of a stock relatively small in relation to the variety of goods handled is an indispensable condition. Those types of retail agencies which have been organized and conducted in recognition of this underlying necessity have latterly prospered and seem most likely to survive.<sup>1</sup> The phenomenal growth of chain-stores, department stores and mail-order houses in recent years evidences the strength of these forces.<sup>2</sup>

<sup>1</sup> An illustration of the rapid expansion of the newer forms of mercantile enterprise is afforded by the record of the Woolworth Company. The average annual increase in the number of stores in this chain for the year 1919 to 1924 was 7.1 per cent, while the volume of sales increased on an average 13.6 per cent per annum in the same time. Since there has been in general a marked decline in the level of prices over this period the difference of 6.5 per cent in the average annual rate of increase of stores and gross sales may be taken to be due in large part to an increase in the rate of turnover. (Figures taken from *Commercial and Financial Chronicle*, January 31, 1925, Vol. 120, p. 579.)

That this rapidity of expansion is not the result of a violent outburst of speculative enthusiasm but has a sound business basis is indicated by the sustained advance of this organization over the period of two decades since the incorporation of the company. (First incorporated, February 14, 1905. See *Commercial and Financial Chronicle*, Vol. 93, p. 2267.) At the reincorporation in 1911 a number of smaller chains were amalgamated with the Woolworth enterprise to form an organization controlling approximately 600 stores. Since that date the expansion has been steady and fairly continuous.

<sup>2</sup> To show that the experience of the Woolworth organization, while perhaps exceptional, does not represent an isolated instance, similar data have been collected for five chains representing as many different lines of trade. The group consists of The Great Atlantic and Pacific Tea Company, J. C. Penney, Owl Drug Company, United Cigar Stores Company, and S. S. Kresge. The number of stores in these five chains increased 55 per cent in the period 1919-1924, while their volume of sales increased 68 per cent. The mounting rate of turnover which, in the absence of contrary evidence, these percentages may be taken to indicate, would have been even more strikingly shown were there some satisfactory basis for adjusting the annual volume of sales to take account of the deflation in the general price level. It may be noted also that the difference between these percentages of growth would have been even greater but for the fact that one of these chains recently adopted an agency policy. The United Cigar Stores Company has made arrangements with some 1200 retail establishments whereby the latter may handle the goods of the United Company under its name, while maintaining their status of independent merchants in other respects. This would naturally be reflected in a lower average sales volume per distributive unit for this chain, even though it might substantially increase the rate of profit on the invested capital.

Into the causes of these far-reaching transformations it is unnecessary here to make an extensive inquiry. But to forestall possible misunderstanding of the relation of this commercial revolution to the standards of competitive business practice, it may be appropriate to indicate briefly the major forces underlying this development. Improvement in the means of communication and transportation furnishes the key to the modern commercial revolution. The ease and advantage of rapid communication by telephone, telegraph, and mail, and the economy of sales-solicitation through the columns of advertising media having wide distribution,<sup>1</sup> have not entirely eliminated personal salesmanship, but they have undoubtedly been working in that direction. Likewise the promptness of delivery by railroad and motor-truck and the dispatch in manufacture itself to which these with other devices contribute have not eliminated the storage of finished goods, but they have greatly reduced the requirements of warehousing. The ratio of the average stocks of finished goods held in process of market distribution to the total turnover of goods for any given period tends in nearly every line of trade to decline.<sup>2</sup> There is less and less reason for distributors to assume the risks of style and price changes, involved in accumulating reserves of merchandise, not to mention the burden of sheer "carrying charges," such as interest, insurance, and depreciation, upon these stocks.

#### §4. SIGNIFICANCE OF RECENT CHANGES IN COMMERCIAL ORGANIZATION

It is only latterly coming to be appreciated that these changes signify more than a modification in the administrative policies of established mercantile distributors. They signify radical rearrangements in the whole trade structure. They account fundamentally for the gradual decline, or eclipse, of jobbing. They account for the confusion and

<sup>1</sup> National circulation magazines, for example, are economical for advertisers not only because of the great number of potential buyers reached by a single advertisement but particularly because their use jointly by a large number of separate concerns, often representing diverse lines of industry, reduces considerably the cost to each.

<sup>2</sup> This is the fundamental explanation of much of the current lament in commercial circles over "hand-to-mouth buying."

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anxiety among regular retailers. They account for the expansion of chain-stores and for the growth of mail-order houses and department stores. Above all, they account for the extension of the manufacturer's activities marketwards and the corresponding multiplication of his problems.

### (a) *Disappearance of Personal Factor in Trade Relations*

The assumption by the manufacturer of some of the functions formerly discharged by a string of distributors was an inevitable outcome of the fundamental changes above described, and would in itself have created difficult problems in marketing technique. But this development meant far more than a simple transference of functions. The transference involved the necessity of introducing a great range of new devices for securing and retaining trade under market conditions devoid of the stabilizing influence of personal relationship. For while improved facilities of communication and transportation have, in the exaggeration of popular phrase, been "annihilating time and space," they have by that token either reduced or mechanized the personal contacts in trade. Business relations which were once suffused with a warm, human quality or atmosphere have become steadily more mechanical and even automatic. Consumers are "sold" on hats, furniture, automobiles, even tombstones, through the columns of their favorite magazines, newspapers, or mail-order catalogues. Even retail distributors are reached by trade journals, mail solicitations, and catalogues, or by human automatons representing the real parties in interest. In the wholesale commerce among manufacturers, goods are purchased more and more either through the mechanism of organized exchanges or upon bids to definite specifications. The transaction of business contracts, save of the weightiest and most intricate nature, could not possibly be carried on in more than a fraction of the volume now daily consummated, if personal interview and private negotiation were substituted once more for all the paraphernalia of modern publicity work, large-scale, direct correspondence, and rapid communication at a distance.<sup>1</sup> Just in so far as the development

<sup>1</sup> Cf. G. W. Goodall, "Advertising: A Study of a Modern Business Power," London, 1914, particularly pp. 77-78.

of these modern facilities has minimized the obstacle of distance to commercial intercourse, there has been a tendency towards the restriction of the influence of the personal factor in trade contacts.

This tendency has a two-fold aspect in relation to the development of competitive methods. In the first place, it has diminished the salutary restraints of personal honor, and of personal pride in one's products, on the temptation to overreaching and cheating in trade.<sup>1</sup> It may well be doubted, however, whether this has worked out in any general decline in the standards of business ethics. For the very mechanical character of business operations which has just been described appears to minimize the opportunities for petty cheating and mendacity, which were certainly ample under the traditional methods of transacting trade. Nevertheless, the impersonalization of market processes has undoubtedly afforded cover for business frauds engineered by "fly-by-night" concerns which could not otherwise have flourished even temporarily. The need of protection to legitimate enterprises in every branch of trade against the raids of such intruders is no less manifest than the need of safeguarding gullible consumers.

*(b) Creation of Good-will Capital by Advertising*

In the second place, and more significantly, the tendency towards the restriction of the influence of the personal factor in trade has meant an accentuation of instability in market relations. This has forced upon producers, or manufacturers, the adoption of sundry marketing devices for the development of good-will and the preservation of their competitive interests. Product identification or branding, extensive and persistent advertising, resale price maintenance, guarantee against price decline,—these illustrate some of the modern developments in commercial practice by which manufacturers have attempted to stabilize the demand for

<sup>1</sup> It is impossible to estimate the part played by personal factors of this character in the maintenance of ethical standards in trade relations. Their influence for good is often no doubt exaggerated. Certainly it must be recognized that alongside of manufacturers and merchants of high integrity, there operated a great number of tricksters and sharpsters. These may have been better able to use their bargaining shrewdness in taking advantage of unwary customers than are their successors today under the impersonal conditions obtaining in modern markets.

their products. And in the absence of personal acquaintance between seller and buyer, which is becoming the rule in the modern market, manufacturers may be expected to continue to experiment with and extend the employment of devices such as these for assuring themselves a steady volume of recurring sales. It is a business necessity, under the circumstances. While the effects of these departures from habit or tradition in the commercial world are by no means entirely ill or entirely good, as is usual upon the introduction of new practices into any given sphere of human affairs, problems of adjustment and regulation have arisen.

The popularization of trade names and brands enables the corporate producer to build up a reputation among unknown consumers in distant markets. But the retention of this good-will is dependent upon the maintenance of definite standards of quantity and quality and, in this way, misrepresentation and deceit are discouraged. Moreover, it not infrequently happens that the good-will value of a name or mark becomes so great that numerous allied products are marketed by the same concern to take advantage of this reputation. In such instances any deterioration of even a single one of the "family of products" would tend to impair the salability of all the others. Any temporary gain that might be anticipated from a policy of exploiting the good-will attaching to a particular product by putting out an article of poorer quality than that upon which the reputation of the brand had been established has, under these circumstances, to be heavily discounted. On the other hand, the increased use of brands in the distribution of commodities and their demonstrated potency in attracting trade have encouraged imitation and infringement among a certain element in the business community. Adroitness in devising subtle forms of poaching has been proven to be one way of taking advantage of the increasing significance of good-will capital in modern business. In like manner the proven selling power of advertising may be taken advantage of, so that misrepresentation of goods and disparagement of competitors become far more of a menace than such tactics could have been in the direct dealings characteristic of local markets.

### §5. NATURE AND SOURCES OF PROBLEM OF REGULATION OF COMPETITIVE BUSINESS METHODS

It should be evident from this summary analysis that the cause of the revolution in commercial organization which is in progress is not to be found in any disturbance or dissolution of the standards of fair dealing in trade, as superficial observers sometimes suggest. The causes of the modern commercial revolution lie far deeper, as has been shown. The connection between the recent changes in the organization of trade and the appearance of a wide variety of new methods or tactics in the transaction of business is, indeed, close; but so far as there is a causal relation it runs in the opposite direction. In truth, the evolution of novel, and in some cases questionable, competitive practices in the last quarter century is traceable in large part to the dislocation in the trade structure. Either indirectly or directly, the same fundamental economic forces which intensified competition among manufacturers and led to industrial combination, on the one hand, and to a revolution of commercial organization, on the other hand, are responsible for the emergence of numerous methods of business competition which challenge economic and legal criticism. These transformations sprang initially from improvements in transportation and communication, and it is obvious that they created a new economic situation requiring business adaptations and legal adjustments. Old guide posts, checks, and standards were no longer useful or effective. It became necessary to build up, more or less hastily and often, therefore, imperfectly, new standards and new tests for the regulation of the methods of conducting trade rivalry. It would have been strange, indeed, had the courts and the untried administrative machinery provided by Congress to work out a solution of this difficult problem arrived at once at a sound conception of right practice in respect to every phase of the conduct of competitive business enterprise. The elaboration of rules defining the limits of fair and legitimate business practice under the complex conditions and fluctuating organization of modern commerce must of necessity take time. It is hoped that some contribution to the sound development of these

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rules may be made by a critical analysis of the experience of the past decade in administrative regulation of competitive practices by the Federal Government. Preliminary to this detailed study, however, it will be necessary in the next two chapters to examine more particularly the nature and results of the regulation of competitive tactics under the common law, and to review the circumstances leading to the establishment of the Federal Trade Commission in 1914 and the general nature of the authority conferred upon it.



## CHAPTER II

### THE COMBINATION MOVEMENT, UNFAIR TRADE, AND THE COMMON LAW

#### §1. THE RELATION OF THE TRUST MOVEMENT TO THE CHARACTER OF COMPETITIVE METHODS

The changes in the organization of trade described in the preceding chapter were accompanied, and in some measure influenced, by a revolution in the organization of industry, which likewise profoundly affected competitive relationships. The concentration of control in manufacturing industries gave rise to the so-called trust problem, and the institution of government regulation of business methods is directly related to the development of anti-trust policy. For the combination movement substantially altered the significance of particular competitive practices and introduced others previously unknown. This focused public attention upon the social aspects of methods of competition, which had not theretofore been regarded as other than a question of private rights.

As the facts concerning the combination movement became known through court proceedings and government investigations, the popular belief that the trusts were to a considerable extent the product of unfair competition was strengthened. Some of the trusts which had attained a high degree of control in their respective industries had been conspicuous for their employment of ruthless and oppressive methods in driving out competitors. These methods, particularly those used in the early years of trust development, tended to subvert the normal operation of competitive forces. In several instances there seemed to be ample evidence that independent producers had been eliminated by the crushing, predatory trade tactics, rather than by the superior efficiency, of huge combines.

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But whether and how far unfair competition was responsible for the growth of trusts, it is certain that the spread of the consolidation movement was responsible for the introduction of numerous methods of competition which were generally regarded as unfair. Not that resort to unethical and uneconomic practices for securing trade was by any means confined to the trusts, but their development provided an opportunity for the utilization of destructive methods of competition before that time ineffective and therefore not specifically condemned either by business morality or by legal rules. And on the other hand, the menace of their size no doubt stimulated resort to underhanded and illegitimate tactics by many small-scale independents uncertain of their own ability economically to compete.<sup>1</sup> In two directions, therefore, the destruction of the approximate equality of competitive business units brought about by the trust movement exercised an important influence in modifying the character of competitive methods. But the temptation to cut-throat competitive warfare was particularly strong on the side of the trusts, inasmuch as in their case the prospects of securing or fortifying a monopolistic control of the market were more immediate. The result was the development of intermittent seasons of ruthless competition characterized by nefarious practices peculiar to the new and enlarged scale of business operations.

### §2. TYPES OF UNFAIR METHODS OF COMPETITION EMPLOYED BY TRUSTS

Among the methods of competition which came into prominence with the expansion of the trust movement some were distinctly unethical and were due apparently to no permanent characteristic of the trust form of industrial organization. Espionage, commercial bribery, and direct interference with competitors' sources of supply and customer-relations are simply indefensible practices, the spread of which seems to have been traceable to no other circumstance than the intensification of competitive rivalry. Certainly they were used by small-scale independents as well as by the

*See American Making Co. v. Keital*, 209 Fed. 351 (1913); 217 Fed. 672 (1914).

dominant consolidations. In a milder form they were known before the rise of the trusts and will doubtless always persist to some extent as long as private interest continues to be the organizing force in trade.

Other methods of competition which the growth of trusts stimulated, and which subsequently have come to be regarded as distinctly unfair, if not illegal, were directly connected with the changed industrial situation introduced by trust development. Intimidation by threats of spurious law suits or a ruinous price war, the operation of bogus independents, the use of fighting brands, exclusive dealer arrangements, tying contracts, and railroad discriminations illustrate competitive tactics which were fostered primarily by the disparity of size among competing business units. Some of these are obnoxious, not because of any conflict in their practice with the principles of common morality, but solely because of their tendency under modern conditions to hamper or block the enterprise of independent producers. Such, under certain circumstances, were exclusive dealer arrangements, tying contracts, and railroad discriminations. In order to maintain effective competition in industry these methods were ultimately condemned, and the large combinations were simply deprived of the full leverage of their bargaining power for this purpose. But there was nothing in the use of these methods which could have been regarded as unfair apart from the circumstance of unequal size among the competing business concerns and the incidental consequences upon competition in the market.

The extent to which these various types of unfair competition were employed by industrial combinations cannot be estimated with any approach to accuracy. The various reports of government bureaus and investigating committees by no means exhaust the entire range of the consolidation movement. Some of them, moreover, contain conflicting statements; and alleged facts are not always supported by reliable evidence. In proceedings under the Sherman Act competitive conduct has been subjected to examination and judgment only in so far as it might afford proof of an intent to monopolize. The opinions of the courts in these cases,

accordingly, are inconclusive in respect to the substantiation of many of the specific allegations of unfair practices. Still less conclusive are the numerous quashed indictments and consent decrees which are sometimes relied upon by investigators.<sup>1</sup> Nevertheless, the sum total of the valid evidence is sufficient to indicate the widespread use by industrial combinations of methods of competition corresponding to the types discussed above.

It will suffice to note in this connection the character of the competitive methods employed by a few of the more prominent combinations prosecuted under the Sherman Act. The National Cash Register Company was cited for its employment of intimidation in various guises and of espionage.<sup>2</sup> The American Tobacco was charged with making extensive use of bogus independents and fighting brands, and also with resorting to exclusive dealer arrangements.<sup>3</sup> The Standard Oil Company was cited at various times for its activity in securing railroad rebates and other forms of preferential treatment from carriers, as well as the frequent use of the device of local price-cutting.<sup>4</sup> These combinations were not by any means alone in the employment of such methods of competition. The Whiskey Trust,<sup>5</sup> the American

<sup>1</sup> For example, in "Unfair Competition," by W. H. S. Stevens, Chicago, Ill., 1917, considerable reliance is placed upon these sources.

<sup>2</sup> *U. S. v. Patterson*, 201 Fed. 697 (1912); 205 Fed. 292 (1913); 222 Fed. 599 (1915); *Attorney-General v. National Cash Register Co.*, 182 Mich. 99 (1914).

<sup>3</sup> *U. S. Tobacco Co. v. American Tobacco Co.*, 163 Fed. 701 (1908); *People's Tobacco Co. v. American Tobacco Co.*, 170 Fed. 396 (1909); 204 Fed. 58 (1913); *Monarch Tobacco Works v. American Tobacco Co.*, 165 Fed. 774 (1908); *Whitwell v. Continental Tobacco Co.*, 125 Fed. 454 (1903); U. S. Commissioner of Corporations, "Report on the Tobacco Industry," Part I, Washington, 1909, pp. 21, 96, 310. See, also, Government Exhibit No. 40 in *U. S. v. American Tobacco Co.*, "Transcript of Record," Vol. V, pp. 248-306.

<sup>4</sup> U. S. Commissioner of Corporations, "Report on the Petroleum Industry," Washington, 1907, Part I, p. 22; "Report of U. S. Industrial Commission," Washington, 1900, Vol. I, pp. 719-726, 732-734; "Report on Investigation of Trusts," 50th Congress, 1st Sess., H. R. 3112, Washington, 1889-1890, Vol. IX, pp. 557-561; *Hardy v. Cleveland & M. R. Co.*, 31 Fed. 689 (1887).

<sup>5</sup> This combination seems to have made it a practice to offer special price reductions to the regular customers of competitors. See "Report of U. S. Industrial Commission," Washington, 1900, Vol. I, p. 181. It also devised an elaborate rebate system for securing exclusive dealing. See "Whiskey Trust Investigation," 52d Congress, 2d Sess., H. R. 2601, Washington, 1893, pp. 78-79; also, *In re Greene*, 52 Fed. 104, 115-116 (1892).

Sugar Refining Company,<sup>1</sup> the Eastman Kodak Company,<sup>2</sup> the Du Pont de Nemours Powder Company,<sup>3</sup> the Corn Products Refining Company,<sup>4</sup> and numerous others at some time during their history were charged with using one or another of the types of competitive practices which are now regarded as unfair.

As already noted, some of these practices were particularly effective competitive weapons in the hands of the trusts. The intimidation of competitors either by threats of relentless warfare or by the institution of spurious law suits was not likely to jeopardize broad public interests save when employed by overtowering combinations with large resources against relatively small producers, though the situation might be made very disagreeable for particular enterprisers even when all concerned were of small size. Interference with established business relations was a real menace only under similar circumstances.<sup>5</sup> The operation of bogus inde-

<sup>1</sup> For an interesting case of alleged interference by this company, with a competitor's attempt to secure credit, see: "Hearings, Special Committee on Investigation of American Sugar Refining Co., and Others," House of Representatives, Washington, 1911-1912, Vol. II, pp. 1217-81; and *Pennsylvania Sugar Refining Co. v. American Sugar Refining Co.*, 160 Fed. 144 (1908); 166 Fed. 254 (1908). Regarding local price discrimination, see *U. S. v. American Sugar Refining Co.*, Petitioner's Testimony, Vol. III, pp. 1478-79, 1490, 1497, 1610.

<sup>2</sup> For use of fighting brands, consult *U. S. v. Eastman Kodak Co.*, 226 Fed. 62, 76 (1915); and bogus independents, *ibid.*, p. 74; and interference with competitor's supplies, *ibid.*, p. 71; and exclusive dealing contracts enforced by espionage, *ibid.*, p. 77. See, also, "Report of U. S. Industrial Commission," Washington, 1900, Vol. XIII, pp. 174, 192; *Eastman Kodak Co. v. Blackmore*, 277 Fed. 694 (1921).

<sup>3</sup> W. H. S. Stevens, "The Powder Trust," *Quarterly Journal of Economics* (1912), Vol. XXVI, p. 447. This article quotes from the testimony in *U. S. v. E. I. Du Pont de Nemours & Co.*, 188 Fed. 127 (1911), to show that bogus independents and price-cutting were employed. No specific reference to these practices is made in the reported case. The final decree, however, prohibited such methods. See "Decrees and Judgments in Anti-Trust Cases," Washington, 1918, p. 195, 203.

<sup>4</sup> This company used its secret ownership of a subsidiary as a cover for a cost-or-less price war against the National Candy Co., which had invaded the field of glucose manufacture occupied by the Corn Products Refining Co. The combine also sold starch and glucose secretly through brokers at less than market prices to customers of competitors. In addition, the company devised a long-term profit-sharing plan, so-called, for the enforcement of its exclusive dealing policy. These facts were brought out in proceedings under the Sherman Act, which finally resulted in partial dissolution of the company, *U. S. v. Corn Products Refining Co.*, 234 Fed. 964 (1916).

<sup>5</sup> In *U. S. v. American Can Co.*, 230 Fed. 859, 874-75 (1916), the court declared it was proven that defendant had paid large sums to manufacturers of can-making machinery in consideration of their undertaking not to furnish machines to others, and that defendant had also induced the combination controlling practically the entire domestic production of tin plate not to sell to defendant's competitors save

pendents, the use of fighting brands, and local price-cutting were not feasible except for business concerns with relatively large capital operating in a wide market. They are not adaptable to small-scale industry. To maintain a separate manufacturing organization under concealed ownership required large capital investment. The employment of fighting brands could not long continue without the possession of other brands with good-will value from which the profits might be used to offset the temporary losses on the cut-price brand. Similarly, local price-cutting was suited only for use by a large concern with a wide market against small concerns with narrower markets. Even rebating could be used more effectively by combinations than by independents, because of the leverage which their larger volume of shipments gave them.<sup>1</sup> Moreover, railway discriminations other than direct rebating were within the reach of industrial consolidations, but frequently beyond that of their independent competitors. When indirect rebating came to supplant the earlier discredited practice, the trusts were often in a position, by virtue of their larger operations and the ownership of small switching railroads and private car lines, to secure and conceal very special favors.<sup>2</sup>

at fixed amounts per box, varying according to grade and size, in excess of the prices charged defendant. The testimony showed, moreover, according to the court, that these arrangements constituted an effective check upon rival enterprise; but it is obvious that such interference with supplies could be accomplished only by a large combination whose resources and purchasing power far exceeded those of any other single concern.

<sup>1</sup> For the "evening agreement" between the South Improvement Co., controlled by the Standard Oil Co., and the Pennsylvania Railroad, see: "Report of the U. S. Industrial Commission," Washington, 1900, Vol. I, pp. 610-15, and "Report on Investigation of Trusts," Washington, 1887-1888, 50th Congress, 1st Sess., H. R. 3112, Vol. IX, pp. 357-61. See, also, *U. S. v. Delaware, L. & W. R. R. Co.*, 152 Fed. 269 (1907); *N. Y. Central and H. R. R. Co. v. U. S.*, 212 U. S. 481 (1909); *U. S. v. Standard Oil Co. of N. Y.*, 192 Fed. 438 (1911); and Interstate Commerce Commission, "Twentieth Annual Report," Washington, 1906, p. 41.

<sup>2</sup> For a survey of the various devices latterly employed to conceal unfair discriminations, see: Interstate Commerce Commission, "Twenty-first Annual Report," Washington, 1907, pp. 106-107. In a subsequent report the Commission stated: "We find that a certain number of large industrial concerns control tracks and terminal facilities nominally owned by small railroad corporations which do not rise to the dignity of common carriers. As a result the connecting carriers make a switching allowance or a division of the joint to such terminal lines which in practice results in discrimination and places the industrial at an advantage in the market." Interstate Commerce Commission, "Twenty-fifth Annual Report," Washington, 1911, p. 12. See, also, on this subject an illuminating article by Bruce Wyman, "The Rise of the Interstate Commerce Commission," in *Yale Law Journal*, Vol. 24, pp. 529-543, especially pp. 536-7.

### §3. SCOPE OF COMMON LAW REGULATION OF COMPETITIVE PRACTICES

It is manifest that most of the foregoing types of unfair competition are either relatively innocuous or not adapted for use except in an industrial system organized around large-scale units such as the combination movement developed. But this was not the system of trade and industry which the common law in its formative period was designed to govern. The common law grew up under economic conditions characterized by handicraft production and direct dealings between producer and consumer, mostly in local trade.<sup>1</sup> Its doctrines relating to trade relations were limited, therefore, to such as were appropriate and necessary to the regulation of an industrial system composed of numerous small business units of substantially equal size and having a similar, and restricted, range of operations. While most of these common law doctrines proved to be applicable under the changed conditions brought about by large-scale manufacture and industrial consolidation, they were effective only in so far as they were subjected to steady modification and revision. But quite beyond the reach of these doctrines were many other types of commercial malpractice or unfair competition which were not known or contemplated at the time the common law rules were crystallizing into definite form.

Before particularizing these limitations of the common law rules as applicable to the situation brought about by the growth of machine industry and the combination movement, it is necessary to sketch summarily the outlines of these common law rules. It is impossible to appreciate their limitations without understanding their actual scope. The first problem in this connection is to determine just what principles and rules of the common law are to be considered its measures for regulating trade competition. In a sense and in some degree almost every branch of the common law system affected the organization and conduct of trade. The law of contracts and criminal law, to mention no others, placed some limits upon private discretion in the accumulation and use of capital,

<sup>1</sup> See Frederick Pollock, "The Genius of the Common Law," Part VII, Perils of the Market Place, *Columbia Law Review*, Vol. 13, pp. 1-12.

though in general under the common law a wide latitude in individual choice of means was sanctioned. Of course, one might not steal another's goods, or burn them so as to make one's own more valuable. These and similar restrictions, however, were not directed specifically to traders and to the regulation of ordinary market processes.

But the common law developed some limitations upon economic freedom particularly applicable to the organization and conduct of trade. Even under the simple conditions of trade in markets of narrow compass, where buyers knew sellers personally and all parties had substantially equal bargaining power, the system of free contract had to be protected from self-destruction. While maintaining always liberal encouragement to private enterprise and individual responsibility, the common law really did supply some "rules of the game" for business. These were, for the most part, expressed in doctrines pertaining to the vindication of civil rights of private parties. Individual traders and business concerns were protected against the unbridled aggression of others in so far as such protection was necessary, in a system of small-scale industry and local markets, in order to foster that competition which was implicit in the whole system of the common law as the automatic adjuster of the conflicting interests nurtured by its individualistic emphasis. Obviously the reach of this protecting arm of the law did not need to be far. And it was not. The initial economic handicaps upon independent enterprise being at a minimum, the responsibility of the law was fulfilled by assuring equality of opportunity in trade. Fostering competition indirectly by the provision of a few private remedies for private wrongs, rather than preserving competition by positive measures administered by public authorities, was the burden of legal regulation of competitive practices under the common law. To this end, rights of action were afforded for three more or less distinctive types of injury to business interests from over-zealous enterprise. These were: (1) the deceitful diversion of patronage, (2) the misappropriation of trade secrets, (3) malicious interference with business relations or operations. These will be discussed in order.



(a) *The Deceitful Diversion of Patronage*

Trade-marks, being recognized as a form of property, had long been protected from infringement,<sup>1</sup> but gradually during the nineteenth century this protection was extended to less formal distinguishing features of a firm's product.<sup>2</sup> To create confusion in the minds of buyers by deceptive means and thus secure patronage intended for another was recognized as "unfair trade" or "unfair competition." Not only the simulation of the appearance of a rival's product or business equipment, but also the imitation of a trade name were found to be thus deceptive and were therefore held illegal. Such practices were sometimes known as "passing off," and the condemnation of the law reached every method of effecting sales which exploited the good-will developed by a trade competitor. While there was no exclusive right to geographical names, surnames, common descriptive terms, or decorative colors for use in designating a firm or its products, a concern which employed such a name, term, or color already known in the given trade and connected with another establishment was bound to differentiate itself or its product by appropriate notice.<sup>3</sup> In other words, the law did not require proof of positive fraud in "unfair competition" cases. If the tendency to mislead buyers existed, an innocent intent on the part of the competitor charged with "reaping where he had not sown" would not relieve him from liability. At

<sup>1</sup> *Hogg v. Kirby*, 32 Eng. Rep. 336 (1803); *Coats v. Holbrook*, 2 Sandf. Ch. 586 (N. Y. 1845); *Amoskeag Mfg. Co. v. Spear*, 2 Sandf. S. C. 599 (N. Y. 1849); *Filley v. Fassett*, 44 Mo. 173 (1869), in which the use of the words "Charter Oak" to describe a stove, even separately from the design in which the words appeared in plaintiff's trade mark, was enjoined; *McLean v. Fleming*, 96 U. S. 245 (1877); *Shaver v. Shaver*, 54 Iowa 208 (1880); *Hamilton-Brown Co. v. Wolf Bros. Co.*, 240 U. S. 251 (1916).

<sup>2</sup> *Knott v. Morgan*, 2 Keen 213 (Eng. 1836); *Williams v. Johnson*, 1 R. Cox American Trade Mark Cases, 214 (1857); *Hohner v. Gratz*, 52 Fed. 871 (1892); *Singer Mfg. Co. v. June Mfg. Co.*, 163 U. S. 169 (1896).

<sup>3</sup> *Pillsbury-Washburn Flour Mills Co. v. Eagle*, 86 Fed. 608 (1898); *Walter Baker & Co. v. Baker*, 87 Fed. 209 (1898); *American Waltham Watch Co. v. U. S. Watch Co.*, 173 Mass. 85 (1899); *Shaver v. Heller & Merz Co.*, 108 Fed. 821 (1901); *International Silver Co. v. Rogers Co.*, 110 Fed. 955 (1901); *Elgin National Watch Co. v. Illinois Watch Co.*, 179 U. S. 665 (1901); *International Silver Co. v. Wm. H. Rogers*, 67 Atl. 105 (N. J. 1907); *Herring, Hall, Marvin Co. v. Hall's Safe Co.*, 208 U. S. 554 (1908); *Kansas Milling Co. v. Kansas Flour Mills Co.*, 133 Pac. 542 (Kans. 1913); *J. Kayser v. Italian Silk Underwear Co.*, 146 N. Y. Supp. 22 (1914); *L. E. Waterman Co. v. Modern Pen Co.*, 235 U. S. 88 (1914).

any rate, the continuation of the deception could be prevented on the ground of constructive fraud.<sup>1</sup>

(b) *The Misappropriation of Trade Secrets*

The common law, in the broad sense, afforded redress, also, against the competitive utilization of trade secrets, knowledge of which had been obtained surreptitiously. It appears doubtful that there was any basis for a civil action for damages by one whose business was thus injured.<sup>2</sup> But courts of equity recognized that the unauthorized use of trade secrets, acquired in bad faith, was inequitable and deserving of injunction.<sup>3</sup> This doctrine was originally developed for the protection of secret formulæ and novel methods employed in manufacturing processes.<sup>4</sup> But it was gradually extended in the period under review to encompass confidential information pertaining to commercial operations.<sup>5</sup> In either field of application the law required that a business man should take ordinary precautions not to expose to outsiders what he desired to keep private and confidential. Moreover, a proprietary interest could not be established in a particular method of manufacture or body of market information unless it represented some unique idea or contained some unique facts which set it apart from the common fund of trade knowledge.<sup>6</sup> More important still, it was an essential element in these cases to prove that the defendant had not obtained the information by lawful means.<sup>7</sup> Outright theft or conversion of valuable papers or books would, of course, have constituted a tort; but, in fact, this was rarely the basis of the

<sup>1</sup> Cf. opinion of Justice Holmes, in *Chadwick v. Cozell*, 151 Mass. 190 (1890).

<sup>2</sup> See, however, *Roystone v. John H. Woodbury Institute*, 122 N. Y. Supp. 444 (1910), in which it was declared an action on the case would lie for betrayal of a trade secret.

<sup>3</sup> *Deming v. Chapman*, 11 How. Pr. 382 (N. Y. 1854).

<sup>4</sup> *Morison v. Moat*, 9 Hare 241, affd. 21 L. J. (N. S.) Ch. 248 (Eng. 1851); *Peabody v. Norfolk*, 98 Mass. 452 (1868); *Taber v. Hoffman*, 118 N. Y. 30 (1889).

<sup>5</sup> Compare: *Salomon v. Hertz*, 40 N. J. Eq. 400 (1885), and *Witkop and Holmes Co. v. Boyce*, 112 N. Y. Supp. 874 (1908); 115 N. Y. S. 1150 (1909).

<sup>6</sup> *National Tube Co. v. Eastern Tube Co.*, 69 Ohio St., 560 (1903). Cf. *Bell and Bogart v. Petrolia Mfg. Co.*, 54 N. Y. Supp. 662 (1898), and *Stone v. Goss*, 65 N. J. Eq. 756 (1903).

<sup>7</sup> *Watkins v. Landon*, 52 Minn. 389 (1893); *Fralich v. Despar*, 165 Pa. 24 (1894); *Stewart v. Hook*, 118 Ga. 445 (1903); *Hamilton Mfg. Co. v. Tubbs*, 216 Fed. 401 (1908).

action. In a court of equity violation or procuring the violation of a position of trust and responsibility was viewed in the same light, and as a majority of the cases related to use of secret information secured under previous employment or from former employees, equitable jurisdiction was as a rule invoked. Breach of confidence, accordingly, came to be recognized as the essence of the wrong.<sup>1</sup>

(c) *Malicious Interference with Business Relations or Operations*

A third form of injury to competitive business interests which was included in the category of remediable wrongs at common law was malicious interference with business operations. The scope of common law protection against predatory aggression in trade is difficult to define because of its late development. No longer ago than 1898 it was declared in the House of Lords: "Although the rule may be otherwise with regard to crimes, the law of England does not, according to my comprehension, take into account motive as constituting an element of civil wrong."<sup>2</sup> And in this country similar expressions of judicial opinion have occurred even more recently.<sup>3</sup> This dictum summarizes clearly the traditional attitude of the common law, in the absence of the element of conspiracy, towards injuries deliberately inflicted by means not in themselves unlawful.

*Defamation and disparagement:* Latterly there has been an increasing tendency to condemn malicious interference in the operations of a business enterprise. In other words, certain forms of competitive conduct directed primarily to the damaging of another business enterprise, rather than to the advancement of the doer's legitimate interests, have become the basis of rights of action. For the most part these rep-

<sup>1</sup> *Vulcan Detinning Co. v. American Can Co.*, 72 N. J. Eq. 387 (1907).

<sup>2</sup> Lord Watson in *Allen v. Flood* (1898), A. C. 1, 92. Quoted and criticised by Ames, "Tort Because of Wrongful Motive," 18 *Harvard Law Review*, 411-422.

<sup>3</sup> In *U. S. v. General Electric Co.* (in the U. S. District Court, N. Dist. of Ohio, E. Div., Equity 1051, April 3, 1925) the court said: "In law the motive which moves a man to adopt and follow a course of conduct strictly legal is immaterial and does not render unlawful that which otherwise would be lawful." See, also, *Waterman Co. v. Modern Pen Co.*, 193 Fed. 248 (1911). The opinion in this case has been severely criticised by Wigmore, "Justice, Commercial Morality, etc.," 10 *Ill. Law Review*, 178-189.

resent an extension of established remedies. Thus, defamation was an old legal wrong founded on an interest in personality. It was the invasion of an essentially individual right, for which the law gave redress.<sup>1</sup> So far as trade relations were concerned, malignment of a competitor's character or professional ability alone furnished a basis for a common law action for defamation.<sup>2</sup> But a deliberate disparagement of a competitor's products which implied fraud or dishonesty was considered in the same category as defamation of character and stood on the same footing.<sup>3</sup> On similar grounds an attack upon a business concern's credit was held actionable.<sup>4</sup> This common law remedy was ultimately extended to protect the reputation of corporate organizations.<sup>5</sup> This protection was supplemented by the development of a separate branch of the law generally known by the inappropriate name, Slander of Title.<sup>6</sup> The modern cases in which this doctrine has been invoked have involved mainly claims to patent rights. False statements with respect to the ownership of patent rights furnished the basis of an action for damages. But no action of this nature could be sustained against one who in good faith claimed property or rights alleged to be wrongly used or exercised by his competitor.<sup>7</sup>

<sup>1</sup> See V. V. Veeder, "History and Theory of the Law of Defamation," *Columbia Law Review*, III, 546; IV, 33.

<sup>2</sup> *Garr v. Selden*, 65 Barb. 416 (N. Y. 1848); *Tarleton v. Lagarde*, 46 La. Ann. 1368 (1894); *Mattice v. Wilcox*, 147 N. Y. 624 (1895); *Dancy v. Dancy*, 50 N. Y. Supp. 161 (1898).

<sup>3</sup> *Steketeer v. Kimm*, 48 Mich. 322 (1882); *Lawry v. Raabe et al.*, 89 Cal. 606 (1891).

<sup>4</sup> *Ryan v. Brewing Co.*, 13 N. Y. Supp. 661 (1891); *Brown v. Holton*, 109 Ga. 431 (1899). But see *Stannard v. Wilcox and Gibbs*, 118 Md. 151 (1912), which limits this protection to traders.

<sup>5</sup> *Ohio and M. Ry. Co. v. Press Publishing Co.*, 48 Fed. 206 (1891); *Reporters' Association v. The Sun*, 186 N. Y. 437 (1906); *Pennsylvania Iron Works v. Voght*, 96 S. W. 551 (Ky. 1906). Cf., also, a more recent case, *Shavers Ice Cream Co. v. Polar Products Co.*, 194 N. Y. Supp. 44 (1921).

<sup>6</sup> "This is obviously no part of the law of defamation for the plaintiff's reputation remains uninjured; it is really an action on the case for maliciously acting in such a way as to inflict loss upon the plaintiff." *Hatchard v. Mege*, L. R. 18 Q. B. Div. 771 (Eng. 1887). For a discussion of this particular branch of the law see Jeremiah Smith, "Disparagement of Property," 13 *Columbia Law Review*, 13, 121.

<sup>7</sup> *Hovey v. Rubber Tip Pencil Co.*, 57 N. Y. 119 (1874); *Emack v. Kane*, 35 Fed. 46 (1888); *Electric Renovator Mfg. Co. v. Vacuum Cleaner Co.*, 189 Fed. 754 (1911). Ultimately in the English Courts slander of title was expanded to include disparagement of quality, statements intended to depreciate the quality, merit or value of any person's property. *Linotype Co., Ltd. v. British Empire Type-Setting Machine Co.*, 81 L. T. R. (N. S.) 331 (1899); *Alcott v. Millars' Forests Ltd.*, 91 L. T. R. (N. S.) 722 (1904).

*Inducing breach of contract:* Malicious inducement to breach of contract was another cause of action of modern development based on an ancient action for enticement of servants. There has not, however, been a universal recognition of the principle that interference in contractual relations of others without just cause or excuse is a legal wrong. In some states the precedent of the famous English case of *Lumley v. Gye*,<sup>1</sup> which has been the source of interminable discussion and dispute in this branch of the law, was followed only to the extent of the actual ruling therein.<sup>2</sup> The right of action was limited to deliberate hiring away of the employees or agents of competitors. In other jurisdictions the broad doctrine was developed that the intentional procurement of the breach of an express contract is a wrong, for which damages are recoverable.<sup>3</sup> Another line of authorities, however, repudiated the doctrine of *Lumley v. Gye*, whether in its application to employment contracts or to contracts generally.<sup>4</sup> In these jurisdictions the procurement of the abandonment of an existing contract relationship was regarded as wrongful only when accomplished by illegal means, such as violence, intimidation, or some form of fraud. The courts in this country appear to have been about equally divided between these two positions at the period dealt with here.

<sup>1</sup> 2 El. & Bl. 216; 118 Eng. Rep. 749 (1853). The plaintiff in this case, a theatrical producer, had contracted with a certain Miss Wagner for her exclusive services for a period of three months. The defendant, a competitor, induced Miss Wagner to break this contract. The declaration alleged that the defendant had knowledge of the contract and had maliciously procured its breach. Upon demurrer, the court gave judgment for the plaintiff, but the opinions supporting this judgment revealed disagreement as to the grounds for granting a cause of action. These opinions, nevertheless, uniformly stressed the fact that the defendant's action was malicious. In this connection, a circumstance usually ignored should be noted. The plaintiff had previously secured an injunction against Miss Wagner which prevented her from performing under the direction of the defendant during the term of the contract. *Lumley v. Wagner*, 1 De Gex. M. and G. 604 (1852). Consequently the action of the defendant in inducing Miss Wagner not to fill her engagement with the plaintiff was malicious in the literal sense, no less than in the legal sense. This situation made a case of simple malevolence.

<sup>2</sup> *Haskins v. Royster*, 70 N. C. 601 (1874); *Glencoe Land and Gravel Co. v. Hudson*, 138 Mo. 439 (1897).

<sup>3</sup> *Doremus v. Hennessy*, 176 Ill. 608 (1898); *Beekman v. Marsters*, 195 Mass. 205 (1907); *Bitterman v. Railway Co.*, 207 U. S. 205 (1907); *Tubular Rivet Co. v. Exceter Co.*, 159 Fed. 824 (1908). Among recent cases in agreement are: *Gonzales v. Kentucky Derby Co.*, 189 N. Y. Supp. 783 (1924); *Hat Shop v. Sculley*, 98 Conn. 1 (1922).

<sup>4</sup> *Ashley v. Dixon*, 48 N. Y. 430 (1872); *Boulter v. McCauley*, 91 Ky. 135 (1891); *Boyon v. Thorn*, 98 Cal. 578 (1893).

In general, throughout those jurisdictions following *Lumley v. Gye*, great uncertainty prevailed regarding the circumstances constituting adequate excuse or justification for interference in contract relations to which one was not a party. That the gratification of mere spite or vindictiveness did not constitute such justification seems to have been well established.<sup>1</sup> But did a competitive interest make a good excuse? Taken by itself, the advancement of one's substantial interests in trade competition did not, as a general rule, justify the intentional procurement of a breach of contract between a business rival and some other party, e. g., a customer. It should be added, however, that the mere offer to buy or sell goods in the ordinary course on usual terms addressed to dealers some of whom might be known to have contracts with some competitor of the offeror was not regarded as malicious interference.<sup>2</sup> Some special inducement to break a particular contract was necessary.<sup>3</sup>

*Molestation in exercise of right to do business:* The right to carry on business secure from malicious molestation was a third development in the growth of the common law which marked the period under consideration. The recognition of this right appears to have issued incidentally out of the application of the law of conspiracy in labor cases. But the affirmation of this right was so far from general and its scope and content were so nebulous, owing to its late origin, that it did not, at the time to which this discussion refers, represent an effective bar to the employment of harassing and oppressive tactics in trade competition. There were still

<sup>1</sup> *Moran v. Dunphy*, 177 Mass. 485 (1901). In the opinion per Holmes, J., "It may be taken to be settled . . . that motives may determine the questions of liability, that while intentional interference of the kind supposed may be privileged if for certain purposes, yet if due only to malevolence it must be answered for," p. 487.

<sup>2</sup> *Chambers v. Baldwin*, 91 Ky. 121 (1891); *Sweeney v. Smith*, 167 Fed. 385 (1909), writ of certiorari denied, 215 U. S. 600 (1909); *Citizens' Light, Heat & Power Co. v. Montgomery Light, Heat & Power Co.*, 171 Fed. 553 (1909); *Rosencau v. Empire Circuit Co.*, 115 N. Y. Supp. 511 (1909). See F. B. Sayre, "Inducing Breach of Contract," 36 *Harvard Law Review*, 663-703, particularly pp. 677-683.

<sup>3</sup> This has reference to the situation as it existed roughly during the first decade of this century, and by and large in most jurisdictions. Since then there has been considerable drift toward the doctrine of strict liability for wilful inducement of breach of contract. This is illustrated by the shift in the position of the New York courts. See: *Calvin A. Lamb v. S. Cheney & Sons*, 227 N. Y. 419 (1920); *Campbell v. Gates*, 236 N. Y. 457 (1923); *Gonzales v. Kentucky Derby Co.*, 189 N. Y. Supp. 783 (1924).

ample evidences of the survival in some quarters of the nineteenth century view that, barring the commission of acts positively illegal in their own nature, competition would justify almost any means of getting trade away from others.<sup>1</sup>

The establishment of a competitive business which might under normal competitive conditions impair the trade of an existing concern was not, of course, regarded as wrongful even in those jurisdictions which recognized the right to do business free from deliberate molestation. But when, with the direct object of injuring the plaintiff, a trade competitor offered to do business at ruinous prices temporarily, or made false and misleading representations in its advertising to prejudice the public against plaintiff's goods, or dogged the movements of plaintiff's salesmen and interrupted and annoyed them in their dealings with customers, or induced unconscionable demands to be made upon plaintiff under cover of accommodation extended by him to the general public, or in any like manner evinced a greater concern in causing loss to the plaintiff than in making profits for himself, the courts in some jurisdictions, at least, stood ready to afford relief.<sup>2</sup> As was said in deciding one of an analogous class of cases, "The law views an injury arising from competition differently from an injury done in persecution."<sup>3</sup>

#### §4. FAILURE OF COMMON LAW DOCTRINES TO REACH NEW TYPES OF UNFAIR COMPETITION

While common law remedies for wrongs to private enterprises from unfair competitive practices were available for the correction of certain forms of predatory aggression, it was clear that they could not reach many of the newer types of destructive methods. In particular, such practices as railroad discrimination, the operation of bogus independents, the

<sup>1</sup> *J. D. Park & Sons Co. v. Nat. Wholesale Druggists Assn.*, 175 N. Y. 1 (1903); *Lewis v. Huie-Hodge Lumber Co.*, 121 La. 658 (1908).

<sup>2</sup> *Ertz v. Produce Exchange*, 79 Minn. 140 (1900); *W. Va. Transportation Co. v. Standard Oil Co.*, 50 W. Va. 611 (1902); *Standard Oil Co. v. Doyle*, 118 Ky. 622 (1904); *Evenson v. Spaulding*, 150 Fed. 517 (1907); *Tuttle v. Buck*, 107 Minn. 149 (1909); *Wesley v. Native Lumber Co.*, 97 Miss. 814 (1910); *Dunshie v. Standard Oil Co.*, 152 Iowa 618 (1911); *Boggs v. Duncan-Shell Furniture Co.*, 163 Iowa 106 (1913). See also *American Bank & Trust Co. v. Federal Reserve Bank*, 256 U. S. 350 (1921).

<sup>3</sup> *Mills v. U. S. Printing Co.*, 91 N. Y. Supp. 185 (1904).

use of fighting brands, tying contracts, and exclusive dealer arrangements lay entirely outside the scope of common law regulation. These devices were not directed at the elimination of particular competitors, but were designed to make competition from any quarter difficult. There being no special injury to a particular rival enterprise which could give rise to a private cause of action, the common law afforded no means of regulating them. Other modes of competing unfairly, such as misrepresentation and misbranding, though not directly connected with the combination movement, tended to have the same effect as railroad discrimination, the use of fighting brands and the other practices above mentioned,<sup>1</sup> and they could not be stopped under the common law for like reasons. This situation was well brought out by an oft-quoted opinion of Judge Day, speaking for a federal circuit court all three of whose members subsequently became justices of the Supreme Court.<sup>2</sup> "The theory of the case seems to be," said the court, "that complainant, manufacturing a genuine aluminum (wash) board, has a right to enjoin others from branding any board 'Aluminum' not so in fact, although there is no attempt on the part of such wrongdoer to impose upon the public the belief that the goods thus manufactured are the goods of complainant. . . . Can it be that the courts have the power to suppress such trade at the instance of others . . . in the same business who use only pure aluminum? We find no such authority in the books and are clear in the opinion that, if the doctrine is to be thus extended, and all persons compelled to deal solely in goods that are exactly what they are represented to be, the remedy must come from the legislature and not from the courts."

Even within their well-defined compass the recognized doctrines of the common law, in spite of a considerable elasticity already noted, proved to be not altogether effective in their application to the complex conditions of modern commerce. Some "unfair competition" cases, for example, in view of the current situation, amount to an endorsement

<sup>1</sup> The effect, namely, of enabling producers to secure trade and survive upon some basis other than industrial efficiency and economical administration.

<sup>2</sup> Taft, Lurton, and Day sitting as a Circuit Court of Appeals in the case of *American Washboard Co. v. Saginaw Mfg. Co.*, 103 Fed. 281 (1900).



of subtle forms of poaching. Thus in one notable case an enterprising partnership secured, through a colorable transaction, the right to use the name of one, A. A. Waterman, upon the fountain pens produced by a company of which it was the exclusive sales agency.<sup>1</sup> These "Waterman" pens came into direct competition with the well-known "Waterman's Ideal" pens, manufactured by the L. E. Waterman Company. In an action to prevent the continuation of this fraud the relief was limited to a requirement that the defendant should clearly indicate upon its goods that it had no connection with the L. E. Waterman Company. This was clearly in line with numerous precedents. But it took no account of the modern conditions of sale of this class of goods. The demand is created by national advertising, and purchases are made in thousands of scattered stores. The sales are often made upon description rather than upon inspection and by irresponsible salesmen in no way connected with the producer. Manifestly, the decree did not stop the practice of supplying unsuspecting purchasers in retail trade with the spurious article in response to a request for a "Waterman" pen.<sup>2</sup> Yet it was exactly at this point that the fraud was calculated to take effect. It should be apparent that, while under the "unfair competition" doctrine the primary and fundamental inquiry was whether the facts indicated deception of buyers, the establishment of this tendency was not always sufficient to assure an effective remedy for the wrong.

Again, the common law rule against misappropriation of trade secrets was no bar to espionage. The substance of the offense in this class of cases, for reasons already mentioned, came to be breach of confidence or procurement of breach of confidence. In the words of a New Jersey court in a leading case: "The main ground for relief disclosed by the complainant's case is the existence of inequitable competition arising from a breach of trust, and hence referable to general principles of equity and not to those special doctrines by which unpatented secrets are protected."<sup>3</sup> Obtaining in-

<sup>1</sup> *Waterman Co. v. Modern Pen Co.*, 235 U. S. 88 (1914).

<sup>2</sup> See: J. H. Wigmore, "Justice, Commercial Morality, and the Federal Supreme Court," *Illinois Law Review*, Vol. X, p. 178.

<sup>3</sup> *Vulcan Detinning Co. v. American Can Co.*, 72 N. J. Eq. 387,396 (1907).

formation of the intimate details of a competitor's business by means involving no violation of trust, as, for example, by stealth, does not appear to have been regarded as a basis for legal action. In two cases, at least, the lawfulness of espionage was affirmed.<sup>1</sup>

But perhaps the shortcomings of the common law regulation of competitive conduct were plainest in respect to those practices connected with price-making. The molestation of customers, interference with salesmen, inducement of breach of contract and like means of injuring a rival's trade furnished an adequate ground for legal relief in some jurisdictions, as has been shown, when carried on maliciously. But competitive price-making was sacrosanct under the common law.<sup>2</sup> The assumption seemed to be that this feature of competition could not be abused, save by collusion among sellers against the interests of buyers. It was not conceivable to courts unfamiliar with the changed business situation that its use by a single seller in opposition to the interests of other sellers could possibly be malicious or unjustified. Such practices as local price-cutting or the use of fighting brands were beyond the reach of legal action. The conception of competition implicit in the common law regulations was based upon the philosophy of Hobbes, which resolved life into a struggle for self-preservation. Until this conception had been discredited and a Darwinian view of competition as a selective process to facilitate the survival of the most efficient had gained acceptance, the courts had no rule by which to curb artful discrimination in price between localities or unrestricted price warfare through the medium of selected brands. Meanwhile cut-throat competition in various manifestations was becoming a serious abuse in modern business practice.

The failure of the common law in these several respects to guard the competitive process from unfair and predatory tactics was only partially, however, due to its substantive shortcomings. To an extent the failure of common law regulation was connected with its method. Under the common

<sup>1</sup> *Park & Sons v. Wholesale Druggists' Ass'n*, 175 N. Y. 1 (1903); *Rosky Mt. Bell Telephone Co. v. Independent Telephone Co.*, 31 Utah 377 (1906).

<sup>2</sup> "There is nothing to prevent an individual from selling any property that he has at any price he can get for it," *Walsh v. Dwight*, 40 N. Y. App. Div. 513, 516 (1899). See, also, *Passaic Print Works v. Ely & Walker Dry-Goods Co.*, 105 Fed. 163 (1900).

law the administration of such rules as there were upon unfair competition in trade devolved wholly upon the courts. But the courts are not organized for vigilance. They are ill equipped for detecting or anticipating abuses of privilege; their main function is the vindication of rights and the redress of wrongs. Thus, with the expansion and increasing complexity of modern business, the legal regulation of trade conduct was bound to grow more and more inadequate. The establishment of administrative regulation of business methods came to be generally regarded as an indispensable development if the competitive system was to remain the chief reliance for the ordering of industry and trade.

## CHAPTER III

### DEVELOPMENT OF LEGISLATIVE AND ADMINISTRATIVE REGULATION OF COMPETITIVE METHODS

#### §1. UNFAIR COMPETITION UNDER THE SHERMAN ACT

In the national sphere, the positive regulation of competitive practices was not, with minor exceptions, undertaken until 1914, when the Federal Trade Commission Act and the Clayton Act were passed.<sup>1</sup> Prior to this legislation, Congress had prohibited railway discriminations in the Interstate Commerce Act of 1887, a prohibition which was supplemented by the Elkins Act of 1903.<sup>2</sup> The receiving as well as the giving of rebates or other special favors from carriers was forbidden. By the fifteenth section of the Mann-Elkins Act of 1910 the disclosure by common carriers of information regarding freight shipments which might, in the possession of competitors, be used to prejudice of interests of a consignor was made illegal.<sup>3</sup> Aside from these instances, there was no direct declaration of federal policy in regard to competitive methods in interstate trade up to 1914.

But the Sherman Anti-Trust Act of 1890 provided, as ultimately interpreted, an indirect regulation of competitive

<sup>1</sup> The Federal Trade Commission Act became a law on September 26, 1914 (63d Cong. Chap. 311; 38 Stat. at Large 717). The enactment of the Clayton Act followed shortly, on October 15, 1914 (63d Cong. Chap. 323, 38 Stat. at Large 730).

Among the states there had been some attempts at regulation a little earlier. A notable instance was New Jersey. See N. J., Laws of 1913, Chaps. 13, 14, 15, 16, 17, 18, 19. The statutes of ten states having laws against "unfair competition," though most of them were of very limited scope, were read into the Congressional Record at the time of the debates on the Trade Commission bill. 63 Cong., 2d Sess., Vol. 51, pp. 12219-20.

<sup>2</sup> Interstate Commerce Act, 24 Stat. at Large 379-387. Sections 2 and 3 prohibit respectively unjust discrimination among persons and unreasonable preferences among persons, localities, or kinds of traffic. The Elkins Act, 32 Stat. at Large, 847, in addition to making the receiving or solicitation of rebates or preferences unlawful, changed the penalties for the offense.

<sup>3</sup> 36 Stat. at Large, p. 539, 551 *et seq.*

tactics so far, at least, as industrial combinations were concerned.<sup>1</sup> Though the act contained no specific prohibition of unfair practices,<sup>2</sup> under the "rule of reason" enunciated by the Supreme Court in 1911 the business methods of dominant consolidations became of prime significance as evidence of unlawful intent and abuse of power.<sup>3</sup> Aside from their connection with a possibly "unreasonable restraint of trade," many of the methods which were reviewed and criticized by the courts were not unlawful or even reprehensible. Nevertheless, in several important decrees issued between 1911 and 1914 against combinations charged with violation of the

<sup>1</sup> The exact wording of the first two sections of the Act, which comprise all its substantive provisions of general application, was:

"Section 1. Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several States, or with foreign nations, is hereby declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

"Section 2. Every person who shall monopolize or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several States, or with foreign nations, shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court." Act of July 2, 1890. (26 Stat. 209.)

<sup>2</sup> Moreover, there is no evidence that Congress intended to regulate the mode or manner of competition indirectly under this statute. Judged by the contemporary debates, Congress was interested solely in condemning the formation of monopolistic combinations. This view is contrary to that expressed by Professor Allyn A. Young in his articles on "The Sherman Act and the New Anti-Trust Legislation," *Journal of Political Economy*, March, 1915, Vol. 23, p. 201. An examination of the debates, however, reveals a general hostility towards monopolistic combinations based on their supposed power over prices, but no condemnation of aggressive methods in suppressing competition. See, particularly, *Congressional Record*, 51st Congress, 1st Session (1890), Vol. XXI, pp. 2571, 3150.

<sup>3</sup> *Standard Oil Co. v. U. S.*, 221 U. S. 175-6 (1911); *American Tobacco Co. v. U. S.*, 221 U. S. 106, 182 (1911). It is not intended to give the impression that competitive conduct of combinations received judicial notice for the first time in 1911. See, for example, *U. S. v. Patterson*, 55 Fed. 133 (1893). But the opinion of the court in this case well illustrates the cautious judicial attitude earlier held, even in extreme cases, towards the legal attack upon unfair practices under the Sherman Act. "Counts 4 and 9 . . . do allege," said the court, "a purpose of engrossing, monopolizing, or grasping the trade in question. Such being the case, acts of violence and intimidation may be alleged as means to accomplish the general purpose. Instead of lying outside the statute, they may aggravate the offense." *Ibid.* p. 641. It ought to be added that the decrees issued prior to 1911 in proceedings under the Sherman Act are silent in regard even to "violence and intimidation" as weapons of trade warfare. Cf., however, *U. S. v. Workmen's Amalgamated Council* (1893) and *U. S. v. Debs* (1894). "Decrees and Judgments in Anti-Trust Cases," Washington, 1918, pp. 13-16 and 19-22.

Sherman Act the courts took cognizance of competitive practices, and the use of specified methods of unfair competition was enjoined.<sup>1</sup> In many instances these decrees were made with the consent of the defendant and therefore lack the authoritative character of a judgment in contested cases. Nevertheless, they indicate a growing recognition of the importance of unfair competitive practices, not only as evidence of illegal combination, but also as factors in the achievement of undue restraint of trade.<sup>2</sup>

This closer examination of competitive methods on the part of the courts was, however, distinctly limited as a force tending to raise the standards of trade and market conduct. In the first place, this indirect regulation of competitive methods could not begin to operate in a trade until some business concern had actually achieved, or manifested a purpose to acquire, a dominant position threatening the

<sup>1</sup> In addition to the decrees cited below, attention may be called to the opinion in *U. S. v. Hamburg-American Line*, 216 Fed. 971 (1914), in which a combination to fix percentages of traffic was condoned but the use of "fighting ships" condemned.

*U. S. v. General Electric Co.*, Consent Decree, October 12, 1911. Enjoined bogus independents, tying contracts, monopolization of supplies, and price discrimination. "Decrees and Judgments in Anti-Trust Cases," Washington, 1918, p. 267. *U. S. v. American Tobacco Co.*, Final Decree, November 16, 1911. Enjoined bogus independents. *Ibid.* pp. 165, 188-9. *U. S. v. DuPont de Nemours and Co.*, Final Decree, June 13, 1912. Enjoined bogus independents, and predatory price-cutting. *Ibid.* pp. 193, 203. *U. S. v. Burroughs Adding Machine Co.*, Consent Decree, March 3, 1913. Enjoined espionage and inducement of breach of contract. *Ibid.* pp. 457-8. *U. S. v. American Thread Co.*, Consent Decree, June 2, 1914. Enjoined fighting brands, exclusive dealer agreements, intimidation, false statements regarding a competitor's credit, secret rebates, and price-cutting below cost. *Ibid.* pp. 449, 454-5. Decrees containing provisions similar to the foregoing were also issued subsequent to the enactment of the Federal Trade Commission Act and the Clayton Act in cases previously initiated under the Sherman Act. *U. S. v. Great Lakes Towing Co.*, Decree, February 13, 1915, *Ibid.* p. 253. *U. S. v. National Cash Register Co.*, Consent Decree, February 1, 1916, *Ibid.* pp. 315-16, 319; *U. S. v. Corn Products Refining Co.*, Final Decree, November 13, 1915, *Ibid.* pp. 440, 448.

<sup>2</sup> In the American Tobacco Company case, *cit. supra*, the Supreme Court said: "we think the conclusion of wrongful purpose and illegal combination is overwhelmingly established by the following considerations,

"(a) By the fact that the very first organization or combination was impelled by a previously existing fierce trade war, evidently inspired by one or more of the minds which brought about and became parties to that combination.

"(b) Because, immediately after that combination and the increase of capital which followed, the acts which ensued justify the inference that the intention existed to use the power of the combination as a vantage ground to further monopolize the trade in tobacco by means of trade conflicts designed to injure others, either by driving competitors out of the business or compelling them to become parties to a combination." 221 U. S. 106, 182.

maintenance of competitive conditions.<sup>1</sup> And even under such circumstances no means were afforded for reaching deceptive and unfair tactics of small, independent competitors, often the most irresponsible factors in an industry. In the second place, this indirect regulation was ineffective because, in the absence of proof of a general policy of destroying competition, an isolated attack upon specific unfair methods employed by combinations could not be sustained. Since, under the Sherman Act, exclusive dealer agreements, interference in business relations, tying contracts and like modes of conduct were not unlawful per se, the courts generally refused to intervene at the instance of parties claiming specific injury from particular transactions or practices.<sup>2</sup>

## §2. THE GENESIS OF THE 1914 LEGISLATION

In this situation there were elements of dissatisfaction to economic groups of widely separated interests and points of view. The 1914 legislation was, in substance, an attempt to appease this general discontent—to provide a remedy for the shortcomings of the Sherman Act policy, as disclosed by experience. To some, these shortcomings appeared as an emphatic discrimination against large-scale enterprise. From the time of President Roosevelt's second administration there had been an insistent movement among certain industrial leaders for either a legislative or administrative definition of an exact standard of competitive conduct.<sup>3</sup> They urged

<sup>1</sup> *American Sea Green Slate Co. v. O'Halloran*, 229 Fed. 77, 79 (1915); *American Steel Co. v. American Steel and Wire Co.*, 244 Fed. 300 (1916). In the latter case the court overruled a demurrer to the declaration urging that no action lies for unfair competitive practices under the Sherman Act. The court cited the allegation of the formation of defendant as a combination controlling 75 per cent of the total output of nails in the United States. Then, in regard to its competitive tactics, the court stated: "The defendant had a perfect right, for instance, so far as the Sherman Act goes, to undersell the plaintiff in ordinary business competition, or for the purpose of putting the plaintiff out of business. It had no right to do so as part of a plan to drive everybody out of the trade in order to obtain a monopoly for itself which is what is alleged."

<sup>2</sup> *Whitwell v. Continental Tobacco Co.*, 125 Fed. 454 (1903); *American Banana Co. v. United Fruit Co.*, 160 Fed. 184, 189 (1908); *Wilder v. Corn Products Refining Co.*, 236 U. S. 165 (1915).

<sup>3</sup> Among others Mr. George W. Perkins argued in favor of a federal commission which should have power to license interstate corporations and to validate their proposed actions or policies submitted for its examination, providing the proposed conduct did not, in the opinion of the commission or bureau "unreasonably restrain

persuasively that they did not know and could not find out what methods of business were legitimate for them and what methods were illegal. The Sherman Act provided no security, it was contended, to industrial combinations intent simply upon proving their inherent strength in straightforward competition. And as many of the practices which were enjoined after 1911 in proceedings under the Sherman Act were not unlawful in themselves and were consequently not denied to independent competitors, this was regarded as a discrimination against "good," or law-abiding, trusts.

To others—for example, the consumers—the shortcomings of the government policy appeared as an inadequacy of protection against deception and fraud in trade from whatever quarters these might proceed. The common man was interested in low prices, so he was anxious to safeguard and promote active competition. But he was also interested in honest dealing and sound values. In short, the consumer wanted a more vigilant enforcement of competition, but he demanded a competition free of unfair and deceptive practices.<sup>1</sup> This, according to the contention of many representatives in Congress, could not be assured under the elastic interpretation of the Sherman Act announced in the Standard Oil and Tobacco cases in 1911. These decisions, in the view of many Congressional critics, had opened the way to a long process of judicial definition of what might be regarded as "reasonable" business policies and modes of

trade." Hearings before Committee on Interstate Commerce, U. S. Senate, 62d Congress, pursuant to 3 Res. 98, Wash., 1912, Vol. I, p. 1089 *et seq.* A somewhat similar proposal was made by Judge Elbert H. Gary in his testimony at the same hearings, *op. cit.*, Vol. II, pp. 2407-11. This policy had earlier been embodied in a bill in the 60th Congress, S. 6440, at the suggestion of President Roosevelt, upon which hearings were held, but which was unfavorably reported by the Senate Judiciary Committee. Senate Report, No. 848, 60th Congress, 2d Sess. See also, the discussion of the Sherman Act policy in the same vein by James M. Beck, in "Industrial Competition and Combination," published by the American Academy of Political and Social Science, Philadelphia, 1912, pp. 296-303. The report of the Senate Committee on Interstate Commerce to accompany the Federal Trade Commission bill makes brief mention of various opposing theories and movements for amendment of anti-trust policy. Senate Report No. 597, 63d Congress, 2d Session (1914) pp. 10-14.

<sup>1</sup> Outside the sphere of strictly trade competition, it may be noted that labor was chafing at having its "methods of competition" with employers closely scrutinized and severely restricted while, in many instances, the business methods of the employers in trade competition came under federal regulation but slightly. Consult: American Federationist, e. g., Vol. 19, pp. 215-218 (1912).



business conduct. Numerous representatives of the public interest in Congress proclaimed themselves unwilling to leave to the courts this process of definition.

On the other hand, in certain business quarters there appears to have been a wholesome fear that if Congress undertook to regulate competitive methods in detail there would be a bungling interference with business administration, far more burdensome than the uncertainty existing under the "rule of reason" pending its judicial clarification. The ascendancy of the less conservative elements in Congress foreshadowed a legislative program involving a more rigid control of large-scale industry, with definite and inclusive prohibitions. To the large group of business men in question any policy which would offer some latitude in the legal definition of standards of business conduct was preferable to such severity of regulation. For this reason, they lent their support to the policy of commission regulation.

In addition, there seem to have been some business men who were genuinely desirous of effective administrative machinery and the enactment of definite rules for curbing the expansion of what were regarded as predatory business interests. They feared the use of oppressive tactics by the trusts, whose overtowering size loomed as a formidable menace in itself. They sought a further and more explicit prohibition, therefore, of "strong-arm" methods of competition.<sup>1</sup> The creation of an administrative body was likewise demanded, but not so much for advising industrial combinations as to what could be legitimately done under the anti-trust laws, as for preventing unscrupulous aggression.

<sup>1</sup> Consult Hearings before the Committee on Interstate Commerce, U. S. Senate, 63d Congress, 2d Session, in two volumes, Wash., 1914. Vol. II, pp. 1188-9, 1437, *et passim*. The referendum vote taken by the United States Chamber of Commerce, representing the widest range of business enterprise, upon the new anti-trust measures proposed early in 1914 gave results in some respects endorsing the Administration program and in other respects unfavorable. *Ibid.*, Vol. II, pp. 671 *et seq.*, and 1438 *et seq.* Nevertheless this vote was frequently adverted to in the course of the Congressional debates by the sponsors of the Administration bills as an indication of the approving attitude of the mass of small business men. See, e.g., *Congressional Record*, Vol. 51, 63d Congress, 2d Session, p. 11593. But perhaps the ablest and most vigorous presentation of this point of view which could be found is in the paper read by Mr. Bruce Wyman before the American Academy of Political and Social Science, and published in "Industrial Competition and Combination," *op. cit.*, pp. 67-74.

The legislative program which was finally carried through cannot properly be viewed as a realization of the ends sought by any one of these conflicting movements for the amendment of anti-trust policy. It represents, like most legislation, a compromise; it is a partial satisfaction of the demands arising from many sources and many divergent interests. From the point of view of the larger business interests it extended the federal regulation of competitive practices to the smallest business unit engaged in interstate commerce. From the point of view of the smaller business interests, it specifically outlawed certain methods of competition capable, particularly if not only, of effective employment by trusts or mergers in the extermination of their smaller, isolated rivals. From the point of view of the general public, it gave legal sanction to the enforcement of certain standards of honesty and fairness in trade. Finally, the Federal Trade Commission was established at public expense as a tribunal open to anyone engaged in interstate commerce whose trade interests were being encroached upon by the predatory or unfair aggression of rival enterprises. A more detailed description and analysis of the anti-trust legislation of 1914 will at once show the basis for this summary statement and indicate something of the legislative intention in regard to its main provisions, the concrete application of which will be the subject matter of ensuing chapters.

### §3. MAIN PROVISIONS OF THE 1914 LEGISLATION

The Clayton Act, among numerous other provisions not relating to trade competition, in the second section declared unlawful any discrimination in price—except such as might be based upon differences in quantity or quality—between different purchasers of commodities.<sup>1</sup> Another sec-

<sup>1</sup>*Op. cit.*, Section 2. This and the following section are the only provisions really relating to competitive practices except by way of enforcement. (Sections 4, 5, and 11 to 19 inclusive.) Section 6 relates to the treatment of labor organizations under the anti-trust laws, and Sections 20-25 are concerned with the use of judicial process in such cases. Sections 7 and 8 respectively limit intercorporate stockholding and interlocking directorates in certain respects. These are commonly grouped with Sections 2 and 3 as the anti-trust provisions of this catch-all piece of legislation. In a large way this is, no doubt, proper; but it is clear that Sections 2 and 3 regulate methods of competition, while Sections 7 and 8 regulate methods of combination. The only other sections remaining, Sections 9 and 10, deal with certain features of the operation of railroads.

tion, the third, prohibited the use of exclusive dealer agreements or tying contracts, under similar circumstances.<sup>1</sup> This section was an explicit repudiation of a policy previously followed in decisions of the Supreme Court, which upheld such arrangements, at least so far as patentees were concerned.<sup>2</sup> The most significant single section of this 1914 legislation, on the substantive side, was the fifth section of the Federal Trade Commission Act. By this section "unfair methods of competition in commerce" were "declared unlawful." Here was a broad and general enunciation of public policy toward competitive business conduct. It was elastic enough to reach every conceivable variation of fraudulent or predatory aggression upon trade rivals. It was clear and concise enough to furnish a guide to administrative and judicial construction in its application to the complex and shifting situations of modern business.<sup>3</sup> The

<sup>1</sup> *Op. cit.*, Section 3. Perhaps an abridged quotation of this section would indicate its scope and meaning better than an explanation of the indefinite terms by which it is usually described. It reads: "That it shall be unlawful . . . to lease or make a sale . . . of commodities, whether patented or unpatented, for use, consumption, or resale . . . or fix a price charged therefore . . . or rebate upon such price, on the condition . . . or understanding that the lessee or purchaser thereof shall not use or deal in the goods . . . of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, . . . condition . . . or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

<sup>2</sup> See *Henry v. A. B. Dick Co.*, 224 U. S. 1 (1912), and authorities there cited. It may be mentioned that this section as well as Section 2 were penal in character as originally reported in the House, but the penalties were omitted by the Conference Committee (63d Congress, 2d Session, Senate Ref. 585). The Federal Trade Commission Act having been passed prior to the final consideration of the Clayton Act, the enforcement of these sections (2 and 3) was by Section 11 entrusted to the Commission in the same manner as it was empowered to prevent violations of Section 5 of its organic act. Aside from the action of the Commission in issuing administrative orders, observance of these sections is also stimulated by a provision (Section 4) allowing the recovery of treble damages by injured parties, similar to the provision for private remedies in Section 7 of the Sherman Act.

<sup>3</sup> In a spirited debate in the Senate, Senator Cummins who was on the Interstate Commerce Committee, was allowed by the Chairman, Senator Newlands, to answer the attack upon Section 5. The main opposition to the bill seems to have been concentrated on the fifth section which was regarded by several as too indefinite for an administrative guide. Senator Cummins, in response to pointed inquiries, undertook to clarify the phrase "unfair competition" as used by the Committee in the reported bill. He said: "We have chosen to report a rule for the trade commission in the language that has been suggested, namely, 'unfair competition.' It is that competition which is resorted to for the purpose of destroying competition, of eliminating a competitor, and of introducing monopoly. That is the 'unfair competition' in its broad sense which this bill endeavors to prevent." (*Congressional Record*, Vol. 51, p. 11104.) On the very next page of the Record, however, he cited a simple case of "passing off," a simulation of the trade name White Laundry Soap by a manufacturer putting out crystal white Laundry Soap. He then added,

intention of Congress to condemn, not only deceptive practices, such as misrepresentation and simulation of trade marks, but also practices tending to restrain trade and build up monopoly, was plain.<sup>1</sup> The common law doctrine of "unfair competition," on the one hand, and the principles evolved in the enforcement of the Sherman Act as concrete tests of monopolization, on the other, were manifestly the basic criteria for determining the range of the regulation which Section 5 prescribed.

In regard to procedure, the main articles of interest in the 1914 legislation are found in the Federal Trade Commission Act.<sup>2</sup> The first three sections of this Act created the Federal Trade Commission, provided for a working organization, and, transferring to the new commission the records of the Bureau of Corporations, ended the ten-year experiment of that purely investigational body. The entire fourth section was devoted to the definition of terms. The Commission was empowered in Section 5 to enforce the rule against unfair methods of competition by investigation, findings of fact, and orders to cease and desist from practices found to be unfair. A review of the Commission's action by the federal courts was also provided for on appeal either by the respondent or by the Commission, in case of a disregard of its orders. In addition to the establishment of this machinery of enforcement, the Act gave the Commission a variety of administrative powers and duties, under eight headings, relating chiefly to investigation of trade conditions for sundry purposes.<sup>3</sup>

"That is one class of cases to which this standard would apply." This two-fold nature of the regulation prescribed by Section 5 came out in many stages of the debate. But its frequent acknowledgment by the members of the Committee and the subsequent endorsement by both houses of all the essential features of the bill as reported should make clear the intention of Congress.

<sup>1</sup> See: Senate Report, No. 597, 63d Congress, 2d Session, *Congressional Record*, Vol. 51, pp. 11086-90; 11103-16; 12208-22. It is unnecessary here to discuss in detail the legislative history of these acts. That task has been ably performed by a number of writers. For example A. A. Young, "The Sherman Act and the New Anti-Trust Legislation," *Journal of Political Economy*, Vol. 23, pp. 201-220, 305-326, 417-436. See, also, W. H. S. Stevens, "The Trade Commission Act," *American Economic Review*, Vol. 4, pp. 840-55; "The Clayton Act," *Ibid.*, Vol. 5, pp. 38-54.

<sup>2</sup> The Clayton Act provided in Section 11 for the enforcement of its interdiction of certain business practices and arrangements (in Sections 2, 3, 7, and 8) that the Interstate Commerce Commission, the Federal Reserve Board and the Federal Trade Commission should have jurisdiction in their respective fields. A system of procedure was outlined, also, which conforms in every essential respect with that previously established in the Federal Trade Commission Act.

<sup>3</sup> Federal Trade Commission Act, *op. cit.*, Section 6.

#### §4. SCOPE AND SIGNIFICANCE OF THE FEDERAL REGULATION ESTABLISHED

The avoidance of technical legal phraseology in the substantive provisions of these statutes showed the undoubted purpose of Congress to leave to the Federal Trade Commission and the courts the responsibility of formulating the precise limits beyond which private enterprise might not go in its quest of competitive advantage in trade. But an explicit standard was nevertheless provided for the guidance of administrative judgment. The standard set up, i. e., unfairness, was at once ethical and economic. As an ethical standard it prescribed greater honesty in dealings of producers, who commonly operate on a large scale, with consumers, who commonly take relatively small portions of the total output of even one producer. The changes in manufacture and commerce hereinbefore described had rendered antiquated the old rule of "Let the buyer beware." This common law rule no longer provided an adequate safeguard against commercial chicanery and fraud. In consequence, the efficient producers of goods of genuine merit were handicapped in the marketing of their products, and it was in part the object of the enactment of Section 5 of the Federal Trade Commission Act to remove this handicap.<sup>1</sup> By a blanket prohibition of "unfair methods" it was undoubtedly

<sup>1</sup> Senate Report, No. 597, *op. cit.*, p. 13; *Congressional Record*, 63d Congress 2d Session, Vol. 51, pp. 11103-11116. In discussing the scope of the provision Senator Newlands, who took a prominent part in the framing of this legislation, said: "Now, recollect that in all the cases that I have referred to as involving unfair practice there would be a remedy to the individual, either at law or in equity. The difficulty that we find, however, is that owing to the growth of these enormous corporations, which no one wishes to destroy—I am not speaking of monopolistic combinations . . . —it is very hard for the individual to maintain his ground. If you say to him, 'Well, you have a right at law, or a right in equity, which will be enforced'; it means very little to him, because it means the employment of a lawyer against the lawyers of greater skill and repute. It means the collection of evidence. It means a large expenditure.

"Now the society has an interest in these questions. It not only has the interest of protecting an individual against oppression and wrong, but it also has the general interest in the maintenance of good morals." As a concrete illustration of what was proposed, he then referred to the creation of the Interstate Commerce Commission with power to protect the interest of the individual shipper, "because we knew that the mere possession of an abstract right at law meant nothing to him. We placed society between him and the corporation with which he dealt, and we organized a tribunal conducted at the expense of society with a view to seeing that injustice to the individual was not accomplished. We are simply carrying out that rule now with reference to trade." *Congressional Record*, *op. cit.*, p. 11109.

intended to eliminate at least the grosser forms of artful deceit upon buyers by whomsoever practiced and howsoever achieved. The common law protection of individual sellers whose goods were imitated was extended to all sellers whose market might be destroyed or jeopardized by that or other forms of fraudulent misrepresentation.

But the standard of "unfairness" was also adopted as an economic standard. Not only unfairness operating through deceit upon customers, but also unfairness operating directly by oppression of competitors, was brought within the ambit of the law. Indeed, if one may judge from the general tenor of the Senate debates, the primary consideration moving the adoption of this section<sup>1</sup> was the protection of small-scale producers in the competitive struggle. It was believed that numerous predatory competitive practices had contributed an artificial stimulus to the growth of monopolistic combinations, and it was proposed to reach these practices in whatever form they might appear.<sup>2</sup> Thus, exclusive dealing arrangements and local price-cutting, though they could scarcely be termed unethical under the competitive régime, were regarded by Congress as so unquestionably uneconomic that sections specifically denouncing them, which were at one stage removed from the Clayton bill on the ground that they were fully covered by Section 5 of the Trade Commission Act, were later restored in conference.<sup>3</sup> This action may be interpreted as a confession of the fear of Congress that the courts might unduly circumscribe the scope of Section 5, of the Trade Commission Act, e. g., by restricting it to the common law doctrine of "unfair competition." Lest there should, in that eventuality, remain no declaration of legislative disapproval of the oppressive tactics of combinations designed to eliminate troublesome competitors, Sections 2 and 3 of the Clayton Act were made a part of the anti-trust laws. But the definition of these two special types of business

<sup>1</sup> Section 5 was first introduced by the Senate Committee on Interstate Commerce. See: 63d Congress, 2d Session, Senate Report No. 597; and House Report No. 533, particularly the minority views of Mr. Stevens; also, *Congressional Record*, Vol. 51, pp. 10376-78 and 11086-87.

<sup>2</sup> *Congressional Record*, *op. cit.*, pp. 12208-22.

<sup>3</sup> See: 63d Congress, 2d Session, Senate Document No. 585, reprinted in *Congressional Record*, Vol. 51, p. 15637.

practice which Congress regarded as uneconomic was clearly not intended to preclude the regulation of these or similar tactics under Section 5 of the Trade Commission Act. The debates in Congress make it plain that Sections 2 and 3 are properly to be regarded as precautionary measures. Aside from illustrating and emphasizing what was covered by Section 5 the only purpose served by their inclusion in the Clayton Act would seem to be to open to competitors injured by these practices a private remedy, as provided in the fourth section of that act.

#### §5. RELATION OF ADMINISTRATIVE REGULATION OF BUSINESS METHODS TO CHANGES IN ECONOMIC SITUATION

In conclusion, it is appropriate to inquire what is the fundamental aspect of the administrative regulation of competitive practices instituted in 1914. Did it represent a popular revulsion against a supposed decline in trade morals and an increasing nefariousness in trade methods? Or did it, on the other hand, represent an extension at the instance of a disillusioned business community, of legislative and administrative assistance to a reformation of business methods already in process? Or finally, did it represent the minimum concession of business to governmental interference as the choice of a lesser evil? Certainly it was none of these exclusively. But although business men differed widely among themselves with respect to the scope and character of a suitable regulatory policy, it was generally recognized that the conditions of trade competition might well be improved. The old game of "dog eat dog" was becoming generally loathsome, and the handicaps and hindrances it imposed upon industrial and commercial progress were becoming plainly unsupportable. Moreover, the ruthless methods sometimes employed by large combinations against small rivals, along with the petty frauds of small traders and business crooks, had undoubtedly given rise to not a little public indignation. The authoritative regulation of business methods was undertaken in 1914, therefore, because the business world recognized that some measure for the enforcement of the higher standards of "fair play" in

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trade, which were only gradually emerging in actual practice, was unavoidable.

Whence came this movement for higher standards of "fair play" among business men? What were its sources? Into this larger question this is no place to inquire. But a few of the major considerations responsible for the gradual transformation which had come over the attitude of business men toward unfair methods of competition may be merely suggested. The adverse public criticism and the judicial condemnation of the oil and tobacco combinations had been instructive to large-scale industry generally. The obloquy attaching to conviction under the Sherman Act, after "unreasonableness" became an essential factor in the offense, rendered inexpedient and inadvisable resort to repressive policies. The remarkable growth of trade associations in the decade prior to 1914 had tended to foster cooperation and allay the hostility and suspicion engendered by the intense individualism of the nineteenth century. A more pervading influence, hardly less potent than this experience in mutual adaptation, was the general upward movement of prices from the turn of the century. The general downward trend of prices for thirty years following the Civil War provoked recurring spasms of cut-throat price competition, which had not a little to do with the development of trusts. The reversal of this trend shortly before 1900 introduced an era of expansion which had a salutary influence upon commercial ethics. These considerations indicate something of the nature of the forces at work in the business world which fitted in with the movement for the amendment of anti-trust policy, culminating in the enactment of the Clayton Act and the Federal Trade Commission Act.



## CHAPTER IV

### THE REGULATION OF PRICE POLICIES

In considering the concrete development of the administrative regulation of business methods under the federal legislation of 1914, it is expedient to divide the field upon some basis at once readily comprehensible to business executives and appropriate to a study of public policy. Perhaps the simplest method of classifying the specific competitive practices which have come under the scrutiny of the Federal Trade Commission and the courts is to distinguish between practices essentially unethical and practices condemned solely because of their supposed tendency to restrain trade or suppress competition. It is plain that the "unfairness" of some methods of competition, such as misbranding, commercial bribery, and the use of lotteries, derives from the law of fraud. Equally plain is it that other methods of competition, exemplified by exclusive dealer arrangements and resale price maintenance, involve no element of moral turpitude. Their "unfairness" derives from the economic and legal principles supporting freedom of trade and an open market.

This is the broad basis of classification most commonly employed in the analysis and criticism of the rulings of the Federal Trade Commission upon "unfair competition."<sup>1</sup> As has already been pointed out, this two-fold nature of the prohibitions declared in the substantive sections of the 1914 laws was disclosed in the debates attending their enactment. It was implicitly recognized by the Supreme Court in the first important case testing the authority of the Federal Trade Commission.<sup>2</sup> Of the validity of this distinction,

<sup>1</sup> See G. C. Henderson, "The Federal Trade Commission," New Haven, 1924, Chapters IV and V; C. W. Dunn, "The Administrative Application and Judicial Construction of Section 5 of the Federal Trade Commission Act," New York, 1923.

<sup>2</sup> *Federal Trade Commission v. Gratz, et al.*, 253 U. S. 421 (1920). Mr. Justice McReynolds, speaking for the majority of the Court, interpreted Section 5 of the Trade Commission Act as follows:

"The words 'unfair methods of competition' are not defined by the statute and

which corresponds to the division in the criminal law between acts *malum in se* and acts *malum prohibitum*, there can be no question. For certain purposes, notably in considering the elasticity of the prohibitions established, it is undoubtedly useful to distinguish between those regulations of which the legal antecedents are to be found in the law of fraud and those which trace their lineage from the legal doctrine of restraint of trade. There will be occasion to make use of this distinction, therefore, in the course of the discussion of the various practices which have come under scrutiny or been subjected to regulation.

But in studying the relation of the policy of administrative regulation of business methods as instituted in 1914 to the development of business enterprise and the organization of trade, it seems necessary to emphasize the different aspects of business management in which the government regulations take effect. There are certain problems in the control or direction of industrial and commercial establishments in the solution of which the private enterpriser still exercises a free hand. In determining the volume of production, for example, he may, in the absence of conspiracy, act without fear of interference by the government. There are, however, other problems confronting every business man engaged in interstate trade, which cannot be handled safely and intelligently without taking account of the rulings of the Federal Trade Commission. In the main it is to various aspects of the bargaining activities of business men that administrative regulation has been applied. In framing the business policy of a concern with regard to prices, for instance, the rules evolved by the Trade Commission and the courts cannot be ignored. Likewise in devising plans for promoting sales the business manager may find that his discretion is limited by numerous administrative restrictions upon deceit in advertising, premium offers, dishonest packaging and similar matters. Finally, in establishing trade relations with distributors and in adopting a certain policy toward competitors their exact meaning is in dispute. It is for the courts, not the Commission, ultimately to determine as matter of law what they include. They are clearly inapplicable to practices never before regarded as opposed to good morals because characterized by deception, bad faith, fraud, or oppression, or as against public policy because of their dangerous tendency unduly to hinder competition or create monopoly."

the director of a business enterprise must be guided by the settled policies of the Trade Commission in so far as these are sustained by the courts.

In these several spheres the private management of business has been considerably restricted, or circumscribed, by the development of administrative law<sup>1</sup> pursuant to the fifth section of the Federal Trade Commission Act and the eleventh section of the Clayton Act. In order clearly to grasp the significance to business of this extension of government regulation, and in order better to judge its effects upon business enterprise, the specific practices complained of by the Commission will be grouped and studied according to the particular phase of business management to which they relate. Upon this basis, it seems feasible, as suggested, to classify the practices found "unfair" under three major heads. The orders of the Commission relate either to price policies, to sales promotion policies, or to trade relations policies. The order of treatment of the various types of practices which have been attacked will conform to this division.

### §1. PRICE DETERMINATION IN GENERAL

In the main, the price policy of a competitive business remains within the discretion of those responsible for its success or failure. Under the existing economic system this responsibility rests predominantly, if not exclusively, upon those who have risked their capital in the enterprise. It is manifest that private investment in industry and trade cannot, in the long run, be fostered unless the privilege of offering the goods and services produced at voluntarily determined prices is assured. Coercive price-fixing might

<sup>1</sup> The term "administrative law" originally referred to that branch of law, which governed the relations between different departments of government or the conduct of government officials. See: Ernst Freund, "American Administrative Law," *Political Science Quarterly* (1894), Vol. 9, pp. 403-425. With the vast development of commission government in this country since the beginning of the present century the term has come to be applied to the rules or orders of commissions and bureaus. These rulings of administrative tribunals partake of the nature both of legislative enactments and judicial decrees or judgments. Having the force of law, when confined within the jurisdiction of the commission issuing them, they are appropriately and conveniently described as "administrative law." Cf. "The Growth of American Administrative Law," St. Louis Bar Association, St. Louis, 1923; W. H. Pillsbury, "Administrative Tribunals," *Harvard Law Review*, Vol. 36, pp. 405, 583.

conceivably for a time stimulate rather than retard investment in a given industry. High prices and high returns, other things being equal, would attract capital. But coercive price-fixing is arbitrary price-fixing. It affords no assurance that over-investment in any direction will be remedied by the financial readjustment or complete elimination of inefficient concerns, nor that under-investment will be corrected by a price adjustment suitable to the attraction of new capital. As a guide to the distribution of resources among the innumerable alternative avenues of production, no fairly satisfactory substitute has been found for freely determined prices fluctuating in response to the variable pressure of supply and demand.<sup>1</sup>

Experience in the government regulation of railway rates has demonstrated that authoritative price-fixing is not a royal road to an economic utopia. Gouging of shippers, on the one hand, and ruinous rate wars, on the other, may have been prevented. Doubtless these are genuine benefits, so far as they go,—that is to say, considered solely by themselves. But that these results have been attended with waste and comparative indifference in railway management and an uneconomic repression of the transportation industry continuing at one period over many years cannot well be gainsaid. The curtailment of the normal expansion of railway facilities had reached such a stage by 1917 as seriously to impair, and even in some directions to thwart, the national industrial development. The drastic measures adopted during the war to offset this handicap and the weak and inefficient execution of the announced change of legislative and administrative policy in the passage and application of the Transportation Act of 1920 are proof of a fundamental weakness in the policy of government price-fixing. This is not to

<sup>1</sup> For a brief but judicious survey of both American and Allied experience generally in fixing prices of food and other essentials during the war, see: W. C. Clark, "Should Maximum Prices Be Fixed?" *Queens University Bulletin* No. 27, April, 1918.

A passage in the official report prepared for the Committee on Trusts of the Ministry of Reconstruction shortly after the close of the war summarizes very neatly the outcome of war experience in this regard. "Much experience of the control of prices by the State has been gained during the war period. The results have not been such as to leave any widespread desire for its general continuance. . . ." See: *A Study of Trade Organizations and Combinations in the United Kingdom*, London, 1919, p. 127.

condemn, out of hand, the policy of government regulation of railway rates. In that particular field the advantages may outweigh the evils. But it is to emphasize the fact that to such a policy there are shortcomings which one would be sanguine, indeed, to expect time and experience to eradicate. There are certainly few industries, and probably none, in which the conditions are less unfavorable to the successful operation of a system of involuntary price fixation. By far the greater part of the costs of rendering railway service are fixed, i. e., unvarying. Raw materials, which represent the most volatile element in the whole price structure, enter into the operating expenses of railroads only to a relatively slight extent. Fuel is the largest item of this nature, yet it forms but a small fraction of the total cost of the service.<sup>1</sup> Contrasting this situation with that of ordinary manufacturing and mercantile businesses, it becomes manifest at once how formidable must be the difficulties of any attempt arbitrarily to control prices in trade and industry.

Economic theory and practical experience, therefore, both support the general outline of the prevailing policy of the law in leaving to the owners of goods the privilege of offering them in the market at whatever price they severally choose to set, or of refusing to offer them at any price. But to this broad principle have been added certain corollaries, modifications and exceptions. In the sphere of interstate trade these have come chiefly from the legislation of 1914, directly or through regulations made pursuant to its provisions. The principle itself has not been supplanted, but in several particulars it has been so far qualified as to justify a critical examination of the reasons upon which the change in legal policy appears to be based and of the consequences it entrains. There are five principal types of price policy which either have been expressly banned by the anti-trust laws or have been canvassed by the Federal Trade Commission under its blanket authority to prevent "unfair methods of

<sup>1</sup> Thus, in 1923, the fuel cost of Class I railroads in the United States represented only 11 per cent of the gross operating expenses, while wages represented 61 per cent of the total, according to the figures published by the Bureau of Railway Economics. In absolute magnitude an annual expenditure of \$542,000,000 bulks large, but in a total of nearly \$5,000,000,000 it tends to shrink. It should not be overlooked, either, that the gross operating expenses of approximately \$5,000,000,000 by no means cover the total cost of the service.

competition." These are less-than-cost selling; price discrimination; resale price maintenance; basing-point price system; and guarantee against price decline. The scope and effect of these actual or attempted limitations upon the discretionary control of manufacturers and traders over the selling prices of their goods will be discussed seriatim.

## §2. LESS-THAN-COST SELLING

The most far-reaching and most trenchant attempt to delimit private discretion in regard to price quotation was embodied in an early order issued by the Federal Trade Commission against Sears, Roebuck and Company.<sup>1</sup> The findings in this case showed that during the war this mail-order house offered sugar to its customers at from three to four cents per pound. Through its catalogue the respondent represented that because of its large purchases and efficient methods of distribution it was enabled to sell sugar at "less than wholesale price." Actually, it was found, the respondent had lost \$196,000 upon gross sugar sales of \$780,000 during one half year. But sugar was only a "leader," and the offer to sell at a price less than cost (though not so described) was limited to a definite quantity, and even that could be purchased only in conjunction with specific amounts of other groceries. The other goods were so priced as to give the company a profit on the combined sale. On the basis of these facts the Commission issued its order requiring the respondent, among other things, "to cease and desist . . . from selling or offering to sell sugar below cost." Upon petition to the Circuit Court of Appeals the order was modified so as to confine it to misrepresentations regarding the comparative business efficiency and integrity of itself and its competitors.

The broad principle which the Commission here sought to establish, that selling below cost or at unprofitable prices is unfair competition, is clearly questionable. Not only would such a rule stop the use of "leaders" for attracting trade; but it would also prevent the "sacrifice sale" of overstocked merchandise, or the liquidation of financially

<sup>1</sup> *Sears, Roebuck & Co.*, 1 F. T. C. 163 (1918).

embarrassed enterprises. Presumably the Commission did not intend that the principle should be thus rigidly applied, since it would be patently uneconomic from any viewpoint practically to stop entirely the sale of goods which had lost some fraction of their value from style changes or "shelf-wear" in the course of distribution. Something might, indeed, be advanced in favor of the suppression of the practice of offering "leaders" at no-profit prices, whether by manufacturers or by merchants. But the difficulty of administering any such rule must be a sufficient objection to its adoption. How determine the "cost" below which sales prices may not be quoted? If justification might be found in certain commercial contingencies, how ascertain the validity of the claim for exemption? On the whole it should be manifest that any policy of setting minimum standards of price determination must confront no less formidable obstacles than an attempt to enforce maximum price limits, or government price-fixing itself, which is the logical outcome of either policy. These considerations appear to have been recognized by the circuit court of appeals, which upon review amended the order of the Commission so as to forbid only misrepresentation in connection with sales below cost.<sup>1</sup>

Nevertheless, the Commission has not apparently given up entirely the idea that unprofitable selling under some circumstances may be unfair competition. In all, ten other complaints have been issued against the sale of goods on this basis, the latest one in 1923.<sup>2</sup> In two of these cases,

<sup>1</sup> *Sears, Roebuck & Co. v. Federal Trade Commission*, 258 Fed. 307 (1919).

<sup>2</sup> *Ward Baking Co.*, Complaint No. 21, Annual Report, 1918, p. 57. *United Drug Co.*, Complaint No. 32, Annual Report, 1918, p. 58. *American Mailing Device Corp.*, Complaint No. 83, Annual Report, 1918, p. 63. *Cutler Mail Chute Co.*, Complaint No. 84, Annual Report, 1918, p. 64. *U. S. Food Products Corp.*, Complaint No. 338, Annual Report, 1920, p. 122. *The Oakes Co.*, Complaint No. 344, Annual Report, 1920, p. 124. *New England Bakery Co.*, Complaint No. 345, Annual Report, 1920, p. 124. *Crocker Bros.*, Complaint No. 580, Annual Report, 1920, p. 149. *Baltimore & Philadelphia Steamboat Co.*, Complaint No. 869, Annual Report, 1922, p. 135. *Waldes & Co.*, Complaint No. 947, Annual Report, 1923, p. 185.

It may be noted that Complaint No. 580 was issued against a number of importers of ferromanganese for alleged "dumping" in the American market. The practice of "dumping" was made a misdemeanor by the Act of September 8, 1916 (39 Stat. at Large 798, Sect. 801), but no prosecution was instituted in the courts under this statute in this instance. The proceedings against the respondents herein were dismissed in 1922 for failure of proof (Annual Report, 1922, pp. 145-6). This outcome illustrates the difficulty which must ever confront the attempt to prevent traders from selling their goods at prices which to them are satisfactory.

In this footnote and henceforward reference to "Annual Report" is to the reports

however, this was not the major charge of the complaint.<sup>1</sup> Orders to cease and desist from the practice have been issued in only two instances besides the Sears, Roebuck order.<sup>2</sup> These two orders deserve some discussion. In the proceedings against the Ward Baking Company, the Commission found that the respondent had during "periods of several consecutive days" given "to each purchaser of its bread . . . a quantity of bread equal to the amount of bread daily bought and paid for by such purchaser." There were the usual averments, also, of an "intent, purpose, and effect of stifling and suppressing competition." The findings disclosed that competing baking companies operating in the towns in which the respondent conducted its free bread campaign were "injuriously affected" thereby. It may be noted that the campaign was not general, but was conducted in various communities at different times, and accordingly might conceivably have been attacked as local price discrimination. But the Commission made no attempt to restrict either its complaint or its order to this feature of the situation. The original order broadly prohibited respondent from "giving or offering to give free of charge to purchasers . . . of its bread or other bakery products, whether such gift is made for the purpose of advertising respondent's products, . . . or for any other purpose whatsoever, bread or other bakery products." Subsequently the Commission did modify this order to the extent of prohibiting such free bread campaigns only "where such practice is calculated to or does stifle . . . competition"; but the circumstances which would render these campaigns obnoxious were not specified. Thereafter, upon petition to the circuit court of appeals, the amended order was vacated, but simply upon the ground that interstate commerce was not involved.<sup>3</sup>

made as of June 30th each year by the Federal Trade Commission to Congress, pursuant to the provisions of Section 6, Paragraph (f), of the Act of September 26, 1914.

<sup>1</sup> Complaint No. 338 and Complaint No. 344. In one of these cases, that against The Oakes Co., the major charge was espionage upon a competitor's business, and the order to cease and desist, which was ultimately made, 3 F. T. C. 36 (1920), was confined to this practice.

<sup>2</sup> *Ward Baking Company*, 1 F. T. C. 388 (1918); *Waldes & Company*, Complaint No. 947. Order announced in Advance Sheets, January 10, 1925.

<sup>3</sup> *Ward Baking Co. v. Federal Trade Commission*, 264 Fed. 330 (1920).



In the other instance, in which Waldes and Company, a manufacturer of dress-snap fasteners, was the respondent, the issue was not precisely selling below cost, but the essence of the complaint was similar.<sup>1</sup> The evidence disclosed that the goods of competitors in the hands of jobbers were accepted by the respondent in exchange for his own product, and subsequently these were offered to certain customers of the competitors at greatly reduced prices. By the order respondent was required to cease selling snap fasteners made by competitors unless the offer to sell be accompanied by a statement that the "goods so offered are second-hand."

The authority of the Commission to enter orders of the character of the two just described may, pending final determination of the issue in the courts, be seriously questioned. Certainly there is nothing immoral in offering to sell two loaves of bread for the price of one, provided there is no temporary deterioration of the quality or wholesomeness of the product and provided no discrimination is involved. The expediency no less than the authority of the Commission's order in the snap fastener case may also be doubted. If the respondent there had pursued a policy of deliberate disparagement of its competitors' products, there might be ground for complaint. But there is nothing in the findings to indicate, except possibly by implication, that respondent did not sell the competitors' goods in its possession for as high a price as it could realize and represent them to be sound merchandise.<sup>2</sup> Under these circumstances, it would seem that the best corrective to such a business policy as was disclosed by the findings in this case is the risk and burden imposed upon the party accumulating a stock of his competitors' products.

Of a similar nature to the policy of underselling is the policy of bidding up prices of raw materials. The same economic principles apply. In the absence of local dis-

<sup>1</sup> *Cit. supra.*

<sup>2</sup> Upon what ground the Commission could require the respondent to state that these products of competitors which it was selling were "second-hand" is not apparent. As commonly used, this term refers solely to goods which have actually been in consumptive use, or actually been worked up into some more advanced product. There was nothing in the findings to indicate that respondent did not sell the goods in exactly the condition it received them from jobber-customers.

crimination by a concern buying in a wide market area, there would seem to be no valid and workable criterion by which to judge of the legitimacy of such a market policy. In the attempt to impose a limit to competitive bidding for supplies and materials the government must tend to defeat the ends of the very law it invokes. The government cannot at once foster competition and prevent it. The ultimate outcome of a policy which limits the reduction of selling prices, generally, in competition, and likewise limits the bidding up of prices by buyers, is the prevention of competition and the substitution therefor of bureaucratic management of industrial resources. Nevertheless, the Federal Trade Commission has issued in all seven complaints against conduct of this description.<sup>1</sup> Only two of these have resulted in adverse orders, but one is still pending at the moment of writing.<sup>2</sup> Neither of the orders condemning this policy has been reviewed by the courts.

The findings of facts in the two cases resulting in orders to cease and desist, both of which sprang from a single episode, disclosed an exceptional situation for which it may be doubted that the right remedy was found.<sup>3</sup> The Brown Company conducted a rendering establishment located in Trenton, New Jersey. It had entered the Philadelphia market to secure additional supplies of its raw material, animal fats. The several Philadelphia rendering establishments had retaliated by forming the United Rendering

<sup>1</sup> *American Agricultural Chemical Co.*, Complaint No. 79, Annual Report, 1918, p. 63. *Consolidated Rendering Co.*, Complaint No. 145, Annual Report, 1918, p. 71. *United Rendering Co.*, Complaint No. 159, Annual Report, 1918, p. 73. *Armour and Co.*, Complaint No. 163, Annual Report, 1918, p. 73. *Davidson, Levy, Adams Co.*, Complaint No. 674, Annual Report, 1921, p. 130. *Ohio Dairy Co.*, Complaint No. 958, Annual Report, 1923, p. 186. *F. M. Stamper Co.*, Complaint No. 1040, Annual Report, 1923, p. 199.

<sup>2</sup> October, 1925. Complaints No. 79 and 159 were the basis of orders to cease and desist. Complaints No. 145, 674, 958, and 1040 were dismissed. (See Annual Reports, 1920, p. 161; 1922, p. 151; Advance Sheets, October 3, 1924; and Advance Sheets, July 17, 1924.)

<sup>3</sup> *American Agricultural Chemical Co. and the Brown Co.*, 1 F. T. C. 226 (1918). *United Rendering Co.*, 3 F. T. C. 284 (1921). In the formal orders in these cases not only was the bidding up of raw material prices in certain localities forbidden, but the Commission also sought to prevent certain harassing tactics. The United Rendering Company was required to cease and desist from spying upon the agents and employees of its competitors, particularly the Brown Company. And the Brown Company was forbidden to allow the drivers of its trucks to bring about collisions with the trucks of spying competitors which were following them about.

Company and, through it, entering the market for animal fats in Trenton, New Jersey, and other cities in which the Brown Company customarily operated. As a result of the severe competition the Brown Company was driven into bankruptcy, and the American Agricultural Chemical Company eventually came into the conflict as the purchaser of a controlling interest in the reorganized company. The Federal Trade Commission, whether successfully or unsuccessfully does not appear, attempted to end the trade warfare by requiring the respondents each to stop bidding up the prices of raw materials in certain cities, actually those where the other principally operated, to levels "unwarranted by trade conditions and so high as to be prohibitive to small competitors." How compliance or non-compliance with this order is to be determined, it may be left for the Commission to explain. That a federal court would ever attempt to enforce it may well be doubted. It seems plain from the findings of fact that the United Rendering Company was a simple combination in restraint of trade, having for its primary object the exclusion of the Brown Company from the market. Why it should not have been proceeded against on that basis is difficult to understand.<sup>1</sup>

### §3. PRICE DISCRIMINATION

Price discrimination is one of the two trade practices specifically denounced in the legislation of 1914. The selection of this "unfair" practice and exclusive dealer arrangements for particular prohibition is perhaps attributable to a current belief that these two devices were widely and effectively used by trusts to cripple competition in different lines of industry.<sup>2</sup> But though this may have been true in the early period of trust development, local price discrimination, at least, the evil against which the

<sup>1</sup> Among other evidence of the character of the United Rendering Co. in this respect may be mentioned the offer of a bribe of \$35,000 for the withdrawal of the Brown Co. from the Philadelphia territory. This proposition was made to the principal stockholder of the Brown Co. shortly after its forced reorganization, but prior to the acquisition of the controlling interest by the American Agricultural Chemical Co., 3 F. T. C. 284, 292 (1921).

<sup>2</sup> The substance of Sections 2 and 3 of the Clayton Act and their general significance are set out in Chapter III, *supra*.

second section of the Clayton Act was principally directed, seems to have very generally fallen into disuse in later years. Whether owing to the purifying influence of legislation or to the salutary lessons of business experience, this particular practice has nearly, if not quite, vanished from the commercial scene. The Federal Trade Commission has found occasion for issuing only four complaints against this price policy during the ten years since it was organized.<sup>1</sup>

But the condemnation of the business policy of quoting discriminatory prices, in Section 2 of the Clayton Act, is not confined to local price-cutting. In broad and comprehensive terms the statute encompasses personal discrimination of all kinds, as well as place discrimination. To be sure, several exceptions are expressly made, including discrimination for the purpose of meeting competition and discrimination which is merely casual in connection with choice of customers and not in restraint of trade. Whether these exceptions do not negative the rule itself depends upon their interpretation, and there will be something to say on that question presently. Even in the absence of this section, however, it is indubitable that local price-cutting, at least, could have been reached under Section 5 of the Trade Commission Act. Indeed, since 1920 no complaints have been issued charging a violation of Section 2 of the Clayton Act which have not also charged unfair competition under Section 5 of the Trade Commission Act. During the early period, when the Commission seems to have more rigidly distinguished its Clayton Act jurisdiction from jurisdiction under its organic act, several complaints charging price discrimination were based solely upon Section 2 of the Clayton Act.<sup>2</sup> It is significant, however, that in the only one of these cases

<sup>1</sup> *C. L. Coleman Lumber Co.*, Complaint No. 13 (1917), 1 F. T. C. 538 (1918), Dismissed. *Interior Lumber Co.*, Complaint No. 14 (1917), 1 F. T. C. 538 (1918), Dismissed. *Standard Oil Co. of Indiana*, Complaint No. 85 (1918), Annual Report, 1918, p. 64. *International Ice Cream Co.*, Complaint No. 1081 (1924), Annual Report, 1924, p. 219, Dismissal announced April 10, 1925. In the proceedings against the Standard Oil Co. the charge of local price discrimination was incidental to the main charge of enforcing a policy of exclusive dealing among proprietors of gasoline filling-stations. The complaint was subsequently amended and the order issued makes no mention of local price-cutting, 2 F. T. C. 26 (1920).

<sup>2</sup> *C. L. Coleman Lumber Co.*, Complaint No. 13 (1917), 1 F. T. C. 538 (1918); *Interior Lumber Co.*, Complaint No. 14 (1917), 1 F. T. C. 538 (1918); *Galena Signal Oil Co.*, Complaint No. 24 (1918), 2 F. T. C. 446 (1920); *American Sheet & Tin Plate Co.*, Complaint No. 251 (1919), 3 F. T. C. 437 (1921).

resulting in an adverse order the complaint was amended prior to the final hearing in 1920 so as to shift the main basis of the proceedings to Section 5 of the Trade Commission Act.<sup>1</sup> In recent years, in complaints against various forms of price discrimination, a violation of both Section 5 of the Trade Commission Act and Section 2 of the Clayton Act has generally been charged.<sup>2</sup> And in at least one recent case such a complaint appears to have been based exclusively on the general prohibition of unfair methods of competition.<sup>3</sup>

It will be necessary, in the first place, to examine the grounds of the alleged unfairness in price discrimination which brought about its legal prohibition. Is it dishonest, it may be asked, for a seller to take more from one buyer than from another for identical articles sold simultaneously? Has it not been a common method of transacting business for generations to strike an independent bargain in each negotiation? And if the exploitation of some buyers, less crafty than others, occurs, is the seller responsible for their weaknesses? How, under a régime of private property and free exchange, impute moral delinquency to those who take full advantage of the weak bargaining power of other parties voluntarily dealing with them, or of their own superior strength in the market? The answers to these questions depend upon the nature of the discrimination which one has in mind. In general, a barrage of questions such as this is posited on the false assumption that every type and degree of discrimination must be either prohibited or allowed. But only the unwary will permit themselves to be impaled thus on a single horn of a gratuitous dilemma. There is discrimination and discrimination, and as will presently be shown there is absolutely no way of entirely avoiding discrimination in the sale of merchandise. The question becomes one of what kinds and degrees of price discrimination are defensible, in fact and in law; and this means a separate consideration of

<sup>1</sup> *Galena Signal Oil Co.*, cf. F. T. C. Annual Report, 1918, p. 57; *ibid.*, 1919, p. 48 *ibid.*, 1920, p. 158.

<sup>2</sup> See, for example, *The Mennen Co.*, Complaint No. 606 (1920), 4 F. T. C. 258 (1922); and *United States Steel Corp., et al.*, Complaint No. 760 (1921). Order issued July 21, 1924.

<sup>3</sup> *South Bend Bait Co.*, Complaint No. 729, Annual Report, 1921, p. 138, *ibid.*, 1922, p. 154. Cf., however, 4 F. T. C. 355, 1922.

the major types of discrimination which appear in practice and have received the attention of the federal authorities.

(a) *Local Price Discrimination*

The challenge to local price discrimination is not based upon the disparity in treatment accorded different buyers of identical goods under like conditions. That is the basis for the condemnation of rate discrimination by the railroads and other public utilities, and in strict logic it might also justify the requirement of the single price policy in commerce. Actually, however, there are important economic differences between public utilities and ordinary industries, so that this principle has not been extended to commerce generally. The objection to local price-cutting is founded principally upon the *indirect* effect of the relatively low price to some buyers rather than upon the *direct* effect of the relatively *high* price to the remaining buyers. The indirect effect is to draw away customers from competitors of the seller operating in restricted market areas. The relatively low price, where it applies, tends to demoralize their sole market and ruin their business, while the operations of the one practising the discrimination may be only partially affected and the loss suffered only temporary. This, then, is the ground for complaint. Local price discrimination imposes an economic handicap upon small-scale competitors as against their larger rivals, a handicap unrelated to their comparative efficiency.

As has already been pointed out, the employment of this policy, notwithstanding its supposed potency as a means of eliminating competition, appears to be on the wane. It has engaged the attention of the Federal Trade Commission but slightly in recent years.<sup>1</sup> Certain economic features of local price discrimination, not hitherto described, may throw light upon its general abandonment. There exists no surer way of vexing buyers, whether they be ultimate consumers or

<sup>1</sup> In the complaint against the International Ice Cream Co., the respondent, it was charged, "sold its ice cream in Pittsfield and North Adams, Mass., at a price far below the usual and customary price, below the price charged by it in other territories, and below cost, with the purpose and intention of suppressing the competition of the Country Maid Ice Cream Co." This illustrates a tendency quite too pronounced in the drafting of complaints by the Commission to lump indiscriminately together numerous accusations many of which form no essential element of the offense charged. This complaint (No. 1081) was dismissed April 10, 1925.

distributors, than to compel some, in practice usually the majority, to pay more for a product than others, under conditions which suggest favoritism. If the situation of those who pay less for a commodity differs from that of those who are constrained to pay more only by reason of the fact that they are separated by an imaginary geographic line, the sense of unjust discrimination among the latter is, quite apart from the reasonableness per se of the price to them, likely to have repercussions upon their demand for the product. The increasing information about markets which characterizes modern trade at every stage makes this deterrent upon local price-cutting more and more effective.

Special circumstances, moreover, militate against the successful use of this policy in certain industries. In a great many lines of trade, perhaps the majority, even the largest manufacturers continue to sell their products through the regular distributive system, made up of independent merchants. But without complete control of a separate distributive organization, the difficulties of maintaining lower prices for a given product in a restricted area than it is sold for elsewhere are nearly insurmountable. The competitive interests of dealers will tend to obliterate arbitrary differences in price quotations which have no meaning or, at least, promise no advantage to them. In the absence of power legally to enforce prices of resale, the offer of goods to dealers in a restricted area at exceptionally low prices can only have the effect of increasing orders from them for goods to be sold beyond the limits of their usual trade territory at price reductions made possible by the lower cost. Or, if increased orders at the lower-than-usual price are refused, the main object of the policy will be thwarted. It will tend to have no other effect than to enrich the fortunate dealers within the selected area, since there will be no occasion for them to reduce their selling prices. Thus, without a completely controlled private distributive organization, the attempt to hinder competitors by local price-cutting tends to engender active hostility in the trade or else to fail completely.

Another circumstance unfavorable to the adoption of the policy of local price-discrimination in some industries, quite apart from the danger of legal embarrassment, is the "fluid-

ity" of their products. Goods upon which the cost of transportation does not bulk large as an element in the final sales price tend to have a wide market irrespective of the scale of operations of particular producers. In such industries, consequently, the smallest competitor is under no more of a disadvantage by reason of local price-cutting than the large business unit which is the aggressor, other things being equal. Since the products of each are or may be economically sold in a market of equal compass, what is sauce for the one is sauce for the other. Practical considerations such as these have probably had something to do with the lapsing of this device, but its definite prohibition by Congress, with provision of remedies to competitors injured by its employment, may well have had a chastening effect upon those who had otherwise been tempted to use it. And this may be true, notwithstanding the limitations upon the enforceability of the statute represented by the exemption of price-cutting "to meet competition," which seems so far to have effectively blocked its specific application.

*(b) Discrimination Based Upon Trade Status*

The basis for the attempted regulation of the price policy of manufacturers in respect to their treatment of different classes of distributors is quite other than the basis for the prohibition of local price discrimination.<sup>1</sup> The discrimination involved in adopting a given system of classifying buyers and consistently quoting different prices to different buyers on the basis of that classification may conceivably hinder or restrain competition to some extent among the buyers. But it is not apparent how adherence by a manufacturer to any particular policy of trade discounts could in any way unfairly prejudice his direct competitors. If, or to the extent that, the preferences established are recognized by the dealers to be fair, certainly the competing manufacturers have no ground for complaint. If, on the other hand, such prefer-

<sup>1</sup> This statement must not be misconstrued. The legal attack upon the two forms of discrimination is founded upon the same statutory provisions. These are Section 2 of the Clayton Act and Section 5 of the Federal Trade Commission Act (for the texts of which see Chapter III, *supra*). In distinguishing the "bases" of their regulation, however, the reference, as will appear from the subsequent discussion in the text, is to the economic grounds upon which they have been regarded as obnoxious.



ences are unfair to dealer-customers, or are so regarded, competing manufacturers are not handicapped but instead are afforded the best opportunity for extending their sales.<sup>1</sup> This is on the assumption, of course, that the basis of the price differentials established by the given manufacturer is not exclusive dealing or any similar condition directly prejudicial to the trade of competing manufacturers. Such restrictive conditions are neither necessarily nor ordinarily connected with trade discounts and will be separately discussed.

The real basis for the administrative attack upon dealer price discrimination is the same as that for the judicial disapproval of resale price maintenance presently to be considered. It is regarded as a business policy tending to restrain trade among the distributors of the product. But as the legal doctrine of restraint of trade grew up around certain traditional types of business situation involving agreements, contracts, and conspiracies among competitors, the courts have been somewhat perplexed to find grounds for interference with a business policy which, though it may possibly tend to restrain trade in some quarters, is independently established by a single manufacturer. It was a question, moreover, whether the sweeping prohibition of "unfair methods of competition" in the Trade Commission Act was meant to encompass more than business methods and policies directed against the interests of immediate competitors. In the courts, therefore, dealer discrimination based on commercial status has been held thus far to be entirely beyond the reach of administrative regulation or legal control.<sup>2</sup> But the Supreme Court has not yet passed upon the question deliberately, having simply refused writs of certiorari in the two cases squarely presenting the issue; and as the Federal Trade Commission has persistently sought to prevent what it regarded as unfair price discrimination of this type, the subject deserves some analysis.<sup>3</sup>

<sup>1</sup> As was observed by the court in *National Biscuit Co. v. Federal Trade Commission*, 299 Fed. 733 (1924): "It is very apparent that no cracker manufacturer could be prejudiced by the refusal of his largest rival to satisfy customers or prospective customers by granting the discounts desired." p. 740.

<sup>2</sup> *The Mennen Co. v. Federal Trade Commission*, 288 Fed. 774 (1923), *National Biscuit Co. v. Federal Trade Commission*, 299 Fed. 733 (1924).

<sup>3</sup> Other complaints involving simply or primarily arbitrary classification of dealers include: Complaint No. 251, *American Sheet & Tin Plate Co.*, Annual Report, 1919,

The custom of quoting different prices to different distributors based on the wholesale or retail character of the operations of the prospective purchaser grew up chiefly out of consideration for the different scale upon which wholesalers and retailers commonly did business. The wholesalers normally purchased in larger volume and, as this relieved the manufacturer of the expense and trouble of soliciting and attending to a great number of relatively small orders, they commonly received a price concession.

So long as the traditional channels of trade persisted in unimpaired integrity, this policy of making an arbitrary distinction between wholesalers and retailers in price quotations was not ordinarily discriminatory; at least not markedly so. But with the rise of large-scale retailing in various forms and the disintegration of the jobbing trade along sectional and local lines, the volume of purchases no longer corresponded closely with the trade status of the buyer. Strictly from the sellers' point of view, therefore, the advantage of maintaining a price concession in favor of *all* wholesalers against *all* retailers tended to disappear. But there were counter-considerations weighing against the complete elimination of the principle of a wholesale discount. That large-scale retailing organizations, such as department stores and chain stores, were economically entitled to a lower rate than that obtained by their smaller rivals from wholesale dealers was by no means universally granted. Were not the new-type distributors retailers seeking the custom of the same consumers as were catered to by the single store unit with a specialized line of merchandise? Could it be said they were competing on even terms if the chain store, the department store, or the mail-order house got its goods at the wholesale price?

p. 78, Dismissed, Annual Report, 1921, p. 150. Complaint No. 514, *Webb Publishing Co.*, Annual Report, 1920, p. 181, Dismissed, Annual Report, 1920, p. 181. Complaint No. 729, *South Bend Bait Co.*, Annual Report, 1921, p. 138. Order to desist, 4 F. T. C. 355 (1922). Order subsequently rescinded as result of decision in Mennen Case, Annual Report, 1924, p. 191. Complaint No. 781, *Salt Producers' Assn.*, Annual Report, 1921, p. 147, Order to desist, 5 F. T. C. 67 (1922). Complaint No. 1015, *Wm. R. Warner & Co.*, Annual Report, 1923, p. 194, Dismissed Sept. 9, 1925. Complaint No. 1168, *Quaker Oats Co.*, Annual Report, 1924, p. 232. Dismissal announced April 23, 1925, Complaint No. 1169, *The Ralston Co.*, Annual Report, 1924, p. 232, Dismissal announced April 23, 1925. Complaint No. 1171, *Larrows Milling Co.*, Annual Report, 1924, p. 232, Dismissed October 15, 1924. See, also, in this connection, *De Soto Paint Mfg. Co.*, 5 F. T. C. 177 (1922).

Confronted with this attitude among the "regular" distributors who, whatever may be the ultimate fate of the type of commercial organization they represent, are actually the dominant factors in the final distribution of the vast majority of consumable goods, manufacturers in many lines have been bewildered as to what course to pursue. Some have conservatively chosen not to depart from established practice. They refuse wholesale price concessions to any concern dealing directly with consumers, regardless of the size of its individual orders or the volume of its monthly or quarterly purchases. Whether they sell exclusively to wholesalers or in part or wholly through their own distributive organization, manufacturers adopting this policy seek to maintain a uniform price to every branch of the retail trade. They cast in their lot, in other words, with the "regular" distributors.

Such was the policy adopted by the Mennen Company in the distribution of its toilet preparations and which evoked the complaint of the Federal Trade Commission.<sup>1</sup> In that case the specific charge was that the refusal to grant "wholesaler" discounts to a cooperative organization of retail druggists who ordered goods of the Mennen Company in wholesale quantities and stood ready to make any arrangements which the Mennen Company might stipulate regarding prompt and certain payment, constituted an unfair method of competition and illegal price discrimination. The Mennen Company took the ground that the members of such "buying clubs" were the real parties in interest and that as they sold directly to consumers they could not qualify for the wholesale discount. The Commission's order to cease and desist from the pursuit of this policy was reversed by the circuit court of appeals<sup>2</sup> and the Supreme Court refused to review this judgment.<sup>3</sup> The court, however, did not discuss the question of discrimination on its merits as an economic issue. The circuit court simply stated as a fact: "It (the Mennen Company) did not discriminate as between retailers, but sold to all retailers on one and the same scale of prices. And it did not discriminate as between wholesalers but sold

<sup>1</sup> *The Mennen Co.*, 4 F. T. C. 258 (1922).

<sup>2</sup> *The Mennen Co. v. Federal Trade Commission*, 288 Fed. 774 (1923).

<sup>3</sup> *Ibid.*, 262 U. S. 759 (1923).

to all wholesalers on one and the same scale of prices. There is nothing unfair in declining to sell to retailers on the same scale of prices that it sold to wholesalers, even though the retailers bought or sought to buy the same quantity the wholesalers bought."<sup>1</sup> This might be true, but certainly it needs explanation.

Other manufacturers, confronted by the same price-making dilemma springing from the revolution in commercial organization, have chosen an opposite course. By adopting a graduated quantity discount system, they have, whether intentionally or not, cast in their lot with the newer forms of distributive organization. They offer their goods to all buyers indiscriminately at prices adjusted solely to the size of the individual order, or the volume of purchases by a given buyer over a specified period. This policy is manifestly adapted to the interests of chain stores, department stores, and mail-order houses, but experience has demonstrated that there is no way by which a manufacturer of consumers' commodities can entirely avoid partisanship in the lively struggle going on in the mercantile field.

It was such a policy that the National Biscuit Company and the Loose-Wiles Biscuit Company adhered to in the distribution of their bakery products through the grocery trade, and which became the object of complaints by the Federal Trade Commission in 1922.<sup>2</sup> Upon hearing, the Commission found that "the effect of the system of discounts granted by these two companies gives to the chain stores an undue advantage in competing with the independent retail grocers."

. . . It had this result, according to the Commission, because the "chain store systems were allowed . . . to combine the purchases of all the separate units . . ., for the purpose of receiving a larger discount, but the biscuit companies refused to allow associations of independent retailers, . . . to purchase through cooperative purchasing agencies." Moreover, it was found as a fact that the cost of selling a chain system was the same as the cost of selling a number of independent retail stores equal to the number of

<sup>1</sup> 288 Fed., 783.

<sup>2</sup> *The National Biscuit Company*, Complaint No. 836, *The Loose-Wiles Biscuit Company*, Complaint No. 837, Annual Report, 1924, p. 160. Orders issued. Advanced Sheets, Jan. 26, 1924.

unit stores in the chain. For these reasons the Commission held the discount policy of the respondents constituted unfair competition, and was also a price discrimination in violation of Section 2 of the Clayton Act. But the order to cease and desist was, upon review, revoked by the circuit court of appeals;<sup>1</sup> and upon appeal to the Supreme Court a writ of certiorari was refused.<sup>2</sup>

The issue presented to the court may be profitably compared with the issue in the Mennen case. There the question was whether it amounted to an unjust discrimination for a manufacturer to refuse to grant his "wholesale" rate to cooperative retailers' buying organizations. The contention of the respondent was that in reality a buying club composed entirely of retailers was not doing a wholesale business. A distinction between these two categories of traders was held to be justified, and the court went to the trouble of formulating a legal definition of wholesaling and retailing. In the biscuit cases the complaints, accepting the distinction made in the Mennen case, charged that it amounted to unjust and illegal discrimination for a manufacturer to sell at a higher price to one retail organization than to another retail organization ordering goods in like quantities under similar conditions at the same time. But again the court refused to sanction interference with the manufacturer's discretion in pricing his goods to different buyers.

It is impossible to say what was the real basis for this decision. The general tenor of the opinion was to the effect that it was not unfair or unlawful to discriminate between purchasers in large quantities and purchasers in small quantities.<sup>3</sup> But the Commission had not disputed that abstract proposition. It had complained that there was price discrimination among purchasers of the same trade status purchasing in like volume, and that this was unfair. If a cooperative organization of retailers as a business and legal entity is not an unlawful combination under the anti-trust laws, is it not entitled to the full discount upon its aggregate

<sup>1</sup> 299 Fed. 733 (1924).

<sup>2</sup> *Federal Trade Commission v. National Biscuit Co.*, Docket No. 576. Petition denied October 20, 1924.

<sup>3</sup> "The determining factor is the quantity consumed; there is no discrimination among purchasers." 299 Fed., 741.

purchases? The court held that it was not. In the absence of any definite finding that it was an illegal combination or that the discrimination was justified under one of the express exceptions of Section 2 of the Clayton Act, however, the conclusion may be ventured that under the law as now interpreted dealer price discrimination "for any reason or no reason" is exempt from governmental regulation. This view is supported by a remark of the court which may be more significant than its repeated affirmation of the non-discriminatory character of the respondent's discount policy. The court said, "Effective competition requires that merchants have freedom of action in conducting their own affairs." This is reminiscent of the opinion in the case of *Great Atlantic and Pacific Tea Company v. Cream of Wheat Company*, which was a private action brought under the Clayton Act to enjoin a cereal manufacturer from discriminating against a chain store system by refusing to continue to sell its cereal to the plaintiff at the usual car-load rate.<sup>1</sup> The court, in refusing the injunction, declared: "Before the Sherman Act it was the law that a trader might reject the offer of a proposing buyer for any reason that appealed to him. . . . That was purely his own affair, with which nobody else had any concern. Neither the Sherman Act, . . . nor the Clayton Act has changed the law in this particular. We have not yet reached the stage where the selection of a trader's customers is made for him by the government." This is frank, and if it is the law, as now appears, all discussion of the limits of price discrimination among dealers is academic.<sup>2</sup>

In general, it may be observed, no discount plan or price policy could possibly be devised which would not result in some discrimination. If a manufacturer elects to make a uniform price per unit for his product, f. o. b. factory, he discriminates against the large buyers in favor of small buyers. If he adopts a flat discount to all wholesalers, with no concessions to any retailers, he discriminates not only between large wholesalers and small wholesalers, but also between large retailers and small wholesalers. And though he might adopt a graduated scale of discounts based solely on

<sup>1</sup> 227 Fed. 46, 49 (1915).

<sup>2</sup> See Note, 29 *Harvard Law Review*, 77 (1916).

quantity, he would still be discriminating, whether he employed a three-fold or a ten-fold variation of prices, between those buyers barely obtaining a given discount and those falling just short of it. Discrimination in some degree cannot, therefore, be avoided. It is simply a question for each manufacturer of what kind and degree of price discrimination will be least hurtful to his sales. And from the standpoint of public policy the question is whether it is politic to make that choice for the manufacturer or leave it to his private discretion.

In support of the traditional policy of non-interference with the enterpriser in the determination of his selling policy it may be argued that his private interest will lead him to minimize price discrimination among dealers. He cannot afford to antagonize any substantial section of the distributive trade responsible for the final sale of his product. On the other hand, he has every inducement and particularly the inducement of profits to keep the good will of the largest body of dealers whom he can persuade to carry stocks of his product, or rather, perhaps, to keep the good will of the body of dealers who can achieve the largest volume of sales for him. To do this, it may be contended, he will be forced to adopt and adhere to a trade discount policy which will promote the growth of the most efficient distributors. In the second place it may be argued in support of the non-interference policy, that to forbid manufacturers to classify distributors and to deal with certain groups on preferential terms is equivalent to a denial of the right to select their own customers. And aside from the constitutional and statutory protection of freedom of contract there is a grave economic danger lurking in a policy which would make sales to all applicants and on the same terms compulsory. There is an element of credit in almost every business transaction, and to take from a seller the discretionary control over the parties with whom he will deal and the terms on which he will deal with them would be to disregard the sensitiveness of this vital factor in modern commerce.

In opposition to this view of the requirements of sound public policy, there are those who contend that the pursuit of competitive advantage among manufacturers does not in-

variably lead to such treatment of distributors as affords equal opportunity to all to realize the maximum economy of their particular type of organization. In particular, large-scale buyers may be handicapped because the manufacturer is disinclined to make himself dependent upon a few outlets for his products. The greater the number of distributors dealt with, other things being equal, the greater will be the constancy of the flow of orders and the opportunity of stabilizing industrial operations. This has been one of the factors responsible for the development of the tendency toward "direct selling" to retailers, and undoubtedly it has a bearing upon the attitude of manufacturers towards quantity discounts.

There is, in the second place, a tendency in trade, no less than elsewhere in human affairs, toward inertia and the preservation of the *status quo*. Novel methods of marketing have to undergo a probationary period roughly proportioned to the extent of their departure from established tradition. During the period of trial, conservatism and indifference interfere with a just adaptation of policy on the part of those with whom the experimenters must deal, and it is not unusual for active hostility to be encountered.<sup>1</sup> A manufacturer, without even being approached by his regular customers, may refuse to sell to a chain store enterprise at all, or except upon discriminatory terms, rather than risk the ill-will of the great bulk of his distributors. An innovation in mercantile organization tends to solidify the sentiment of those concerns into whose "legitimate province" it "intrudes," and though they may take no positive action to boycott manufacturers

<sup>1</sup> Innovations in business organization and practice do not stand on a peculiar footing in this respect. The same situation confronts adventurers in every sphere of human activity. Numerous illustrations might be drawn from political experience, notably the experiment of republican government begun in 1776. But a most apposite example is afforded by the history of scientific management. Here was an innovation in the organization and methods of production which has had to fight its way forward against formidable obstacles reared by tradition, prejudice, and misunderstanding. The obtuseness of labor leaders, the inertia of business managers, and the perversity of its professed proponents have at times seemed about to engulf the whole movement. Under these heavy handicaps, its progress has been slow. Cf. Frederick W. Taylor, "The Principles of Scientific Management," New York, 1911, F. B. Copley, "Frederick W. Taylor, Father of Scientific Management," New York, 1923; and numerous articles in the Bulletin of the Taylor Society, particularly one in Vol. X (1925), pp. 41-62, "Scientific Management Made Clear," by Irving Fisher.



who deal with the "interlopers," it requires no unusual astuteness in manufacturers to sense their attitude. Under these circumstances, unless his products have an exceptional consumer appeal, the manufacturer will be disposed to maintain a price policy consistent with the best interests of his regular patrons, though this may be prejudicial to the innovator and uneconomic on any broad view of the fundamental features of the situation. The sheer weight of numbers and the authority of tradition, therefore, according to this argument, tend to handicap business concerns undertaking to introduce new ideas in mercantile organization and methods.

It must be recognized that there is some merit in both of these conflicting attitudes toward the case for regulation of price discrimination among distributors. But in the absence of collusion or cooperation between a given manufacturer and a definite group or section of the distributive trade looking to the exclusion or hampering of certain competitors of the latter, it is doubtful if the courts will interfere or sanction interference by the Federal Trade Commission in price discrimination by a manufacturer on the basis of commercial status.

There is one broad fact which is often overlooked in considering this question and which inclines toward the acceptance of the settled legal policy. That fact is the difference in the field of the productive operations of the manufacturer and the field of trading operations of the distributor who handles his product. The product or the line of products of any one manufacturer or any given manufacturing industry represents, in most instances, but a small fraction of the complete range of goods which the distributors handling that product or line of products keep in stock. Thus, linen collars and shirts in their manufacture constitute substantially an independent branch of industry, but in their distribution they form but a relatively minor item in the whole stock, or the gross turnover, of even a modest haberdashery shop. Or, in the grocery trade, canned vegetables constitute a separate manufacturing industry but only a small division of the business of either the wholesale or the retail grocer. This situation is not unique but typical, and it is significant in any considera

tion of the restraint of trade alleged to result from such price discrimination as may be involved in a manufacturer's trade discount policy. Though a given distributor or class of distributors may be somewhat prejudiced by inability to secure supplies of a given manufacturer's product upon fair terms, their business as a whole is not likely to be irreparably injured or indefinitely strangled by the discrimination. Such injury as results may be viewed as incidental to the exercise of the individual rights of the manufacturer, providing always there is no outside coercion or malice involved in the pursuit of the manufacturer's policy.<sup>1</sup>

#### §4. RESELL PRICE MAINTENANCE

Probably no single problem connected with the regulation of competitive methods by the Federal Government has aroused more widespread or determined controversy than that of resale price maintenance. Yet this cannot be attributed to any sudden shift in the law or the attitude of the Government. This practice is one of the few that the Federal Trade Commission has sought to regulate which, in certain forms, had already been held illegal under the Sherman Act. Moreover, it is now held to constitute an "unfair method of competition," in certain circumstances, under the Trade Commission Act also. But no one contends that it is in any way immoral or fraudulent. The sole basis of the legal con-

<sup>1</sup> The same has been said of the right of a wholesaler to refuse to purchase of a manufacturer on account of his policy of selling to chain-stores at wholesale prices. Though the trade of the manufacturer may be injured by such action, it is *damnum absque injuria* in law. In *Raymond Brothers-Clark Co. v. Federal Trade Commission*, 263 U. S. 533 (1924) the Supreme Court, quoting the circuit court of appeals in the same case, stated: "There is no finding that petitioner combined with any other person or corporation for the purpose of affecting the trade of the Basket Stores Co., or others similarly engaged (chain-stores) in business. So far as petitioner itself is concerned it had the positive and lawful right to select any particular merchandise which it wished to purchase, and to select any person or corporation from whom it might wish to make its purchase. . . . It also had the unquestioned right to discontinue dealing with any manufacturer (or in this particular instance with the F. A. Snyder Preserve Company), for any reason satisfactory to itself or for no reason at all. Any incidental result which might occur by reason of petitioner exercising a lawful right cannot be charged against petitioner as an unfair method of competition." Such is the law, and in fact it could hardly constitute a substantial restraint upon the trade of the manufacturer, in this case the Snyder Company, for a single wholesaler, the Raymond Brothers-Clark Company, to decline to deal in its products, in view of the number and variety of competing channels of distribution open to the manufacturer.

demnation is its supposed tendency indirectly to restrain trade. This charge is vigorously disputed by those who defend the practice; but before the judicial and administrative attitude toward this business policy can be understood and intelligently criticized it is necessary to explain its economic characteristics and essential significance.

In general, the policy of resale price maintenance represents an endeavor by a manufacturer to control the price at which his product may be purchased from distributors by consumers.<sup>1</sup> Practically the adoption of such a policy means an attempt to prevent some dealers from "cutting" the standard price announced or advertised by the manufacturer. Why should the manufacturer be interested in maintaining a uniform price to consumers? The answer of the supporters of resale price maintenance is that while the manufacturer is not interested in this per se, he is interested to prevent the depreciation of the good-will attaching to his product in the market from its advertisement at cut-prices. But how can the offer of a commodity at a low price adversely affect its sale?

The answer to this apparently paradoxical question may be found in the nature of the commodities in the marketing of which this policy is alone feasible. Branded or "identified" goods are the only goods susceptible of resale price fixation. Unless an article bears a distinctive trade-mark or trade name there is no means by which the consumer in paying the established price can be assured, except possibly after use of the article, that the dealer may not have substituted similar but inferior products of competing manufacturers. Such potential advantage as a standardized retail price might afford by way of eliminating the irksome necessity of bargaining and thereby encouraging purchases can be realized, therefore, so far as the manufacturer is concerned, only when the standardized retail price applies specifically to his own identified and standardized product.<sup>2</sup> From this it is not to be

<sup>1</sup> It may be noted that the practice sometimes, even frequently, involves control of jobbers' prices to retailers also. But it is obvious that this feature is only incidental to the main end, and the same principles apply to wholesale price maintenance as to retail price maintenance.

<sup>2</sup> On this point, see: C. T. Murchison, "Resale Price Maintenance," New York, 1919, p. 80 ff. This treatise provides the most complete economic analysis of resale price maintenance available. See also: W. D. Moriarty, "The Economics of Marketing and Advertising," New York, 1923.

inferred, however, that the branding of merchandise stands in a direct causal relation to resale price maintenance. Rather it appears that both practices are alike traceable to another factor in the business situation. It is well recognized that the spread of advertising, extensive, intensive, national, producer advertising, mainly accounts for the phenomenal development in modern times of the practice of standardizing commodities and marketing them under distinctive trade-marks. For *producer* advertising cannot be effectively carried on without the adoption of a brand or trade-mark. A business unit which does not deal directly with consumers can secure returns from advertising, commensurate with the cost, only by establishing some means by which its product for sale by others can still be positively identified as of its manufacture.<sup>1</sup>

National producer advertising may not have quite the same close connection with the movement for standardizing the price of manufactured products that it has with the movement for standardizing their quality and identifying their source. But the causal sequence, according to one view, exists even though it follows a less direct course. Advertising may not make resale price standardization imperative, it is admitted, but it makes the practice very advantageous.<sup>2</sup> The argument is that the nature of advertising is such that its full value cannot be realized without reducing to a minimum the friction of actual selling. Dealing, as the advertiser does, indirectly with prospective purchasers, the success of his efforts depends upon the subordination of salesmanship. Bargaining must be as far as possible eliminated. The theory is that the "buying impulse" awakened by an advertisement must not be allowed to "grow cold," as it is said, by any delay or interference in the selling process. The subtle, sensitive, and extremely tenuous complexion of mind induced

<sup>1</sup> For example, while a single coffee-roaster might advertise extensively to stimulate the public consumption of that beverage and would presumably share in the increased demand, he would not find such a policy profitable in all likelihood, unless perchance he already controlled a large fraction of the business. The question of the advantages of cooperative advertising is in no way related to the present discussion.

<sup>2</sup> Producer advertising is what is primarily referred to here, as elsewhere in the ensuing discussion. It may be pointed out, moreover, that the type of advertising had in mind is the ordinary display advertising. What is said applies in some degree, also, to the purely educational type of advertising, but not to the same extent. See G. H. Montague, "Should the Manufacturer Have the Right to Fix Selling Prices?" *Annals American Academy*, Jan., 1916, p. 55.

by advertising must be protected from the destructive shafts of counter-suggestion. The ideal of the advertiser, one is assured, is to make selling an automatic operation. It is manifest, however, that so long as any essential element of the bargain which the consumer must make to possess himself of the advertised commodity, such as the price, remains indeterminate, the mechanization of retail distribution will be incomplete and the ideal of the advertiser unrealized. For to whatever extent judgment, comparison, evaluation enter into the selling process proper, to that extent is the force of advertising dissipated. Likewise the influence of salesmanship tends to be magnified, under these circumstances, to a corresponding extent.

It may be observed that this does not mean that every advertiser endeavors to avoid the entrance of judgment or comparison into the choice of the advertised goods. The educational type of advertising may actually stimulate a qualitative comparison and foster an informed judgment of merchandise. This is generally conceded. But the selection of the given brand of goods advertised is, still, sought to be induced by the advertisement, or at least to be determined prior to the actual entrance of the prospective buyer into the market, and the selling effort of the distributor reduced, thus, ideally to zero. For while the prospective buyer is being "waited upon," so to speak, by the advertisement, the advertiser can control absolutely the mode of dealing with him. As soon as this agent has accomplished his function, however, and the well-disposed consumer is turned over to another agent, viz., the retailer or his clerk, the advertiser can no longer control the suggestions that will be brought forward and he distrusts naturally this irresponsible agent. Accordingly, whether it be an automatic reaction or a reasoned decision that is fostered, the aim of effective advertising is definitely to determine the reader's choice. To this end it is requisite that the advertised article shall have not only a standard quality, a standard size, and perhaps a standard style, but also a standard price.<sup>1</sup> This is one

<sup>1</sup> See E. S. Rogers, "Predatory Price Cutting as Unfair Trade," *27 Harvard Law Review* (1913), 139-158, particularly p. 151 and following; and H. R. Tosdal, "Price Maintenance," *American Economic Review* (1918), Vol. 8, pp. 23-47; 283-305; cf. particularly p. 31 and following.

explanation of the persistent contention of the manufacturers for the privilege of fixing a standard resale price for their products. Fluctuating and variable prices impair the value of producer advertising.

But according to another view, more commonly adopted by the manufacturers themselves, the fact that variable retail prices constitute an obstruction to sales is the lesser of the evils connected with them. It is not the offer of identical goods at different prices itself that is objected to, but the advertisement of a branded product at less than the regular market price. In this way, it is held, the consumer good-will built up by the producer through large investment in national advertising is pilfered, deliberately converted to his own use, by the price-cutting merchant. He utilizes the standardized product under a well-known brand as a reduced-price "leader," to deceive the public into believing that he offers exceptional values in all the goods he sells. He thus uses the manufacturer's property—the good-will acquired by expenditure in advertising—to advertise his own business. The branded product, of course, offers the only practicable, or at least by far the most serviceable, medium for this process, inasmuch as the doubts and suspicions concerning quality which the advertisement of very low prices would otherwise induce cannot arise with respect to the standardized, trademarked article. It is claimed, however, that this appropriation of the manufacturer's good-will to attract customers to a cut-price store does not, and is not intended to, have the effect of augmenting the sales of his identified product. On the contrary, since there is little or no profit, or even a loss, on the "leader" at the advertised cut-price, its sale is not actively encouraged. In trade language, it is not "pushed," even by the merchant who uses it as advertising "bait," and in many cases its purchase may be discouraged.<sup>1</sup>

An even more serious injury results, it is contended, in that sales of this same brand elsewhere tend to be hampered and even destroyed. The attitude of the great majority of

<sup>1</sup> In undertaking these advertised cut-price sales, merchants sometimes subject themselves to the hazard of taking large losses through large sales without profits. An advertising broadcast can be based upon a very restricted offering of goods. Unfortunately, these cut-price sales are too often accompanied by some form of sharp practice, such as substitution of other brands, etc.

distributors toward price-cutting is, of course, one of bitter denunciation. They assert that consumers regard them as "profiteers" when they offer at its standard price the identical articles which the price-cutter is offering at a much lower one. They lose not only the sale of the branded product but customer good-will as well. Consequently, they condemn the vigorous price competition of certain retailers, particularly chain and department stores, and are loath to handle branded goods without some assurance from the manufacturer that the dealer's margin of profit will be protected. The manufacturers of such goods, being largely dependent upon the established channels of distribution, are disposed to give the desired protection. For even though the sales to price-cutters might in some instances increase as a result of the low price at which the product was offered, this would still be an inadequate offset to the decrease in sales to other distributors. Individually the amounts marketed through small, independent stores may not be large, but collectively these stores constitute the chief outlet for trade-marked merchandise. Resale price maintenance is resorted to by the manufacturer, thus, in order to prevent the debasement of his trade-mark and in order to secure dealer cooperation.<sup>1</sup>

On the other hand it is held by some that the whole truth lies not with either of the foregoing considerations exclusively. The real question, it is contended, is as to which jeopardizes less, or safeguards more, the public interest: price-cutting or maintaining standard retail prices. Are the manufacturers' interests in advertising values and dealer cooperation, admittedly legitimate in and of themselves, superior or subordinate to the interests of merchants in liberty of trade? The final test, it is believed, must be the effect upon the general interests of consumers of protecting one special interest rather than the other, for plainly these two special interests are incompatible. As to the consumer's immediate interest in low prices it is admitted that, assuming no price agreements among manufacturers, the final retail price fixed by the producer will be no higher, in so far as it is determined with reference to the fraction realized by himself, than would be the price exacted in the absence of resale price

<sup>1</sup>See opinion of Judge Rogers in *American Tobacco Co. v. F. T. C.* U. S. Circuit Court of Appeals, 2d Circuit, Oct. 20, 1925.

fixation. Another way of stating this same idea would be that the manufacturer will be constrained under this policy to fix a final price that will yield him, for his share, a return no higher than that which he would demand in the absence of this policy.<sup>1</sup> If genuinely competitive conditions obtain in the manufacturing branch of the industry, it may be counted upon that the portion of a fixed resale price going to the manufacturer will, in the long run, be just adequate to cover his costs of production, including such profits as are necessary to induce him to remain in the industry. In so far as this basic factor influences the standard price, therefore, it may be doubted whether fixed resale prices would tend to be higher than the prices resulting from sales without reservation or condition by the manufacturer and open competition among distributors.

But there are other elements in the final price to the consumer besides the return realized by the manufacturer. In the absence of resale price maintenance these other elements representing the wholesalers' and retailers' margins will vary according to the costs of distribution under different systems and even according to the relative efficiency of different dealers operating within any particular system. These margins will constantly tend under pressure of competition to adjust themselves to the most economical level upon which the bulk of the consumer demand can be reached. This need not be in all cases the absolute minimum "spread," or margin, for which any portion of the output can be transferred from the manufacturing plant to the hands of the consumer. But it will in all cases take account of the varia-

<sup>1</sup> Some qualifications on this general proposition may be necessary to cover special circumstances. For example, it is conceivable that the intensified competition among retail dealers, under conditions of non-standardized prices or unenforceable standardized prices with attendant price-cutting in some quarters, may be reflected in such pressure upon the manufacturer as to result in net prices to him yielding a lower margin of profit than the economic normal. If the commodity happens to be one produced under joint cost, this situation may continue indefinitely. Another circumstance which might bring it about that the net price to the manufacturer for a product sold at a fixed resale price would be somewhat higher than the price realized in the absence of such a price policy is the fact that, for convenience to all parties, the standard resale price is normally fixed at a round figure or with reference to coin denominations. If the long-run normal competitive price at retail of a certain article were 23 cents, it is conceivable that the fixed resale price might be set at 25 cents, to the advantage of all parties, and the manufacturer absorb a portion of the extra margin.



tions in actual expense incurred in the distribution of particular portions of the product. The final price will tend, in every instance, to reflect: (a) the relative distance of the consumer from the point of origin of the goods; (b) the extent and nature of the supplementary services furnished by the merchant, e. g., credit, delivery, repairs, shopping conveniences, etc.; and (c) the individual efficiency of the merchant in respect to the basic factors of mercantile management: stock-turnover, clerical expense, rent, and the like. It is charged by those opposed to the practice that the policy of resale price maintenance not only ignores all of these competitive influences in distribution, but arbitrarily suppresses all price differentiation based upon them.<sup>1</sup> The consumer advantageously located with reference to the point of manufacture is constrained to help pay the freight bill properly chargeable to the remote consumer.<sup>2</sup> The consumer patronizing an establishment affording the minimum of service conveniences is obliged to pay as much as another patronizing a more luxurious establishment. But, above all, the customers of efficient and progressive merchants are compelled by the resale price maintenance policy to forego the legitimate advantages which might otherwise be offered them.<sup>3</sup> Thus not only these customers but these merchants are held to be injured by the practice.

<sup>1</sup> It has been contended that the uniform margin prescribed for dealers will tend to be high enough to satisfy the dealers of relatively slow turnover and low efficiency. See W. H. Stevens, "Resale Price Maintenance," 19 *Columbia Law Review* (1919), pp. 265-285. That the amount of gross profit allowed the dealer on the basis of the suggested resale price is frequently excessive cannot be denied. For specific cases see table showing cost, margins of profit suggested, and cut selling price in fourteen stores for thirty-three articles, in U. S. 63d Congress, 2d and 3d Sessions, Hearings on H. R. 13305, "To Prevent Discrimination in Prices and to Provide for Publicity of Prices to Dealers and the Public," Washington, 1915, p. 105.

<sup>2</sup> The market area is sometimes divided into two or more "zones" in which different resale prices are sought to be enforced. This only qualifies the principle stated in so far as it limits the amount of price discrimination. It does not affect the principle in substance.

In the case of the great majority of articles in which this question is at issue the freight item is probably negligible. In the others which are exceptional, such as automobiles, the price is usually based upon some single shipping point.

<sup>3</sup> The absolute importance of these factors affecting distribution costs is minimized by those who favor the price maintenance policy. Some indication of the possibilities of price differentiation on the basis of mercantile efficiency is afforded, however, by the reports of the Harvard Bureau of Business Research upon costs in different lines of distributive trade. In 1923, of 499 retail shoe firms reporting their operating expenses to the Bureau, 16 reported a gross margin upon net sales amount-

Against these considerations the proponents of a privilege to manufacturers to control resale prices point out certain advantages to the consumer of such a policy. The standard price is to an extent a marketing convenience. Travelers buying an article in places where they are unfamiliar with dealer reputations, purchasers who have no time to "shop" or whose faculties from youthfulness or age are inadequate for self-reliance in bargaining—these find protection and security in standard retail prices. The question here is, whether the fraction of the total consumer demand represented by these elements is so considerable, or their interests so paramount, as to justify the permission to impose limitations upon distributive competition? And if, for this purpose, limitations are to be imposed, it is asked whether they had not better come from the government than from the initiative of producers? Moreover, the legal enforcibility of a fixed resale price policy would prevent "profiteering" or undue price increases locally and temporarily. It would be to the manufacturer's interest to make the standard resale price of his product the maximum price. But the opponents of the resale price maintenance policy ask if it is necessary for this purpose to make the announced standard price the *legally enforcible* maximum price, let alone the *legally enforcible minimum* price? They suggest that the same end, namely, the prevention of individual exploitation, may be achieved by the advertisement of what is regarded by the manufacturer as a fair standard price, or by simple announcement, as by stamping it on the package. The consumer who could not protect his own interests under such circumstances does not deserve protection, in their opinion.

The strongest emphasis has been placed by manufacturers upon the view that the denial of the privilege to control the resale price of their identified products opens the way to un-  
 ing to 40% or over, while 22 reported a gross margin of less than 20%. *Bulletin No. 43*, Cambridge, 1924, p. 22. Of 471 retail grocery establishments reporting for the same year, the range of gross margin was from less than 12% to more than 27%. *Bulletin No. 41*, Cambridge, 1924, p. 27. Of 290 firms operating retail jewelry stores, which reported for 1923, 17 had a gross margin of more than 50% and 19 of less than 25%. *Bulletin No. 47*, Cambridge, 1924, p. 29. The range of the gross margin ratio among department stores was not so great, but was striking, nevertheless. Of 403 establishments, all with annual sales below \$1,000,000, there were 33 which reported a gross margin in excess of 34% and 32 which reported gross margin of 21% or less. *Bulletin No. 44*, Cambridge, 1924, p. 32.

scrupulous dealers to trade illicitly upon the good-will developed by them through advertising and reputation. When a dealer selects a trade-marked article as a "leader" and advertises it for sale at a greatly reduced price,<sup>1</sup> the impression is created among consumers, it is averred, that the standard price is an arbitrary or unfair price. An unfavorable opinion is formed not only of dealers who may continue to offer that article at its usual price, but of the manufacturer who advertises it at that price, which now appears extortionate. The "leader" comes quickly to be shunned, one is assured, even in the cut-price establishment itself, as being a questionable value.<sup>2</sup> And after having ruined the salability of one trade-marked article, the unscrupulous dealer then resorts to another for his "leader" which again soon gives place to still another, as each in turn becomes unattractive to consumers. The injustice of this depreciation of established good-will for the purely private and temporary advantage of the distributor is vigorously pressed by manufacturers.

That the policy of some retailers in cutting prices upon trade-marked merchandise does often injure the manufacturers thereof appears to be well established.<sup>3</sup> These dealers,

<sup>1</sup> Sometimes the "leader" policy leads to the quotation of prices at less than the cost to the distributor, but these instances are probably infrequent. In any case, no-profit prices have much the same effect as prices below cost. An analysis of 100 instances of price-cutting advertisements of Colgate products showed only 13 cases in which the goods were offered at less than cost. See testimony of Mr. S. M. Colgate before the Federal Trade Commission, quoted in *Women's Wear*, November 2, 1917, p. 3.

<sup>2</sup> It has been suggested, however, that this result is probably confined to articles, the genuine merit of which does not warrant the price fixed as standard. See: F. W. Taussig, "Price Maintenance," *American Economic Review*, March, 1916, Vol. VI, No. 1, pp. 170-184.

<sup>3</sup> In the hearings before the House Committee on Interstate and Foreign Commerce on the Stevens Bill to legalize price maintenance a statement was submitted by the Secretary of the Kolynos Company in which it was claimed that price cutting had injured the manufacturer through the refusal of dealers to handle the product. Extracts from sixteen letters received from the dealers were given in support of this statement. It was also claimed that at one time the company's sales in Portland, Maine, suffered severely as a result of price cutting by the local stores of the Riker-Jaynes chain system. "Every dealer in town refused to sell Kolynos because they claimed there was no profit for them in handling it. As a result our sales in Portland were greatly curtailed. Not until the price was raised to a higher level did the sales resume their normal proportion." U. S., 63 Congress, 2d and 3d Sessions. Hearings on H. R. 13305, "To Prevent Discrimination in Prices and to Provide for Publicity of Prices to Dealers and the Public." Washington, 1915, pp. 115-116. See also, to the same effect, testimony of Mr. Sidney M. Colgate before the Federal Trade Commission printed in *Women's Wear*, Nov. 2, 1917, p. 25. Mr.

on the other hand, claim they would be injured in their competition with other and less efficient merchants if they were denied the right to quote prices reflecting their ability to operate on a smaller margin of profit per unit of sales. They dispute the contention that their cut prices are purely deceptive advertising "bait" for attracting patronage to their stores. It is not their fault, they say, that they constitute the minority of distributors so that the reaction of the majority of distributors in refusing to stock goods subjected to this vigorous competition results in loss of sales to the manufacturers concerned. It appears to them as an unavoidable incident of economic progress in mercantile methods.

This presents the crucial issue of resale price maintenance. Here are two conflicting interests—that, on the one hand, of the manufacturer interested in maintaining the wide distribution of his products and the good-will and confidence of consumers toward them, built up by large investment in advertising, and by reputation based upon quality and service; and that, on the other hand, of distributors, and through them of customers, interested in securing the reward of independent efficient management of their business. Both interests are real, yet both cannot be satisfied. The question is as to which, according to sound public policy, should be preferred. The answer must depend fundamentally upon the view taken of the function and importance of distribution in the present economic system, and the lines along which it is to develop. Manufacturers, through advertising, have reached out to assume a share of the responsibility for marketing their products. The continuance, i. e., the profitable discharge, of this responsibility necessitates a considerable degree of control over the distributive mechanism. Among other things it involves, as has been shown, resale price control. The tendency is, under these conditions, for the distributive system to become essentially an agency of manufacturers. Some merchants fit into this transformation complaisantly. Others assert their independence and seek to

H. B. Cheney, testifying before the Trade Commission, stated that in one instance as a result of temporary price-cutting the demand for one of his products in a particular market was reduced to one-third of its normal amount. *Ibid.*, Oct. 4, 1917, p. 2.

tie the consumer good-will to themselves, or to their establishments.<sup>1</sup> They resist the forces set in motion by extensive producer advertising. They count upon inducing consumers to trust to their (the merchants') judgment of merchandise and their business integrity rather than to place reliance upon the manufacturers' brands and advertising claims.<sup>2</sup>

Without venturing to take sides in this controversy, it may be observed that if manufacturers are in fact forced to assume the risks and responsibilities of agency in dealing with distributors, as a condition of securing the advantages of such incidents of agency as price fixation, they are not thereby being subjected to any new and unusual burden.<sup>3</sup> Moreover, the special privileges of the legal relationship of agency may well be found, eventually, for this purpose as they have for so many others, abundantly to warrant the bona fide assumption of its obligations. If there exists a real economic basis for the enormous advertising expenditures by which manufacturers endeavor to weave bonds of consumer good-will which stretch over the heads of distributors, can it be doubted that the protection of those tenuous threads by the creation of true forms of agency, or the exten-

<sup>1</sup> This conflict of interest is even more pronounced when the buyers whose resale price the manufacturer attempts to control are themselves further manufacturers, rather than simply distributors. Thus in the case of the *Goodall Worsted Company* (Complaint No. 976, Annual Report F. T. C., 1923, p. 189) the respondent manufacturer of "Palm Beach" cloth was charged with fixing standard prices at which clothing made from this trade-marked product should be sold to jobbers or retailers. Since the market prices of such suits would normally be determined quite as much with reference to their cut, style, finish, and the reputation for workmanship of the tailoring establishments making them up, as upon the quality of the cloth, it is obvious what effect the permission to enforce the resale price maintenance policy would have upon competition in the cutting trade. Incidentally, also, this case furnishes a striking illustration of the arbitrary interference with market price adjustments involved in the resale price maintenance policy. The case is, at the present writing (October, 1925), still at issue.

<sup>2</sup> "I mentioned the fact that the interests of the merchant and the consumer are closely interwoven. It is a well-known fact that the purchasing public look to the merchant whom they patronize and in whom they have utmost confidence to protect them against extortionate prices and undependable merchandise; and, in the event of the purchase of an article which afterwards proves unsatisfactory, they seek redress from the retail merchant without thought of the manufacturer." Testimony of Mr. E. L. Howe, Secretary-Treasurer of the National Retail Dry Goods Association, before the House Committee on Interstate and Foreign Commerce. U. S. 64th Congress, 1st Session, Hearings on H. R. 13568, "Regulation of Prices," Washington, 1916, p. 287. On the other hand, it is asserted that such claims are usually passed on by the merchant to the manufacturer who is ultimately responsible.

<sup>3</sup> Cf. *U. S. v. General Electric Co., et al.* On the U. S. Dist. Court for the N. Dist. of Ohio, E. Div., Equity 1051, April 3, 1925.

sion of industrial integration marketwards, will be justified? This, at least, appears as a possible "way out" of a troublesome situation for the manufacturer, whose interest in the wide distribution of his product gives him a stake in the continued success of small, scattered, independent retail stores. The "independence" of regular retailers would be measurably limited by this development, but there is nothing to indicate that the majority of them would resist or suffer by the transformation.

In the courts, the policy of resale price maintenance has been carefully scrutinized from the beginning. The judicial restraint has gone as far as seemed feasible without trenching upon that irreducible minimum of private discretion which is associated with the ownership of property. Aside from several early cases in the lower federal courts,<sup>1</sup> decided before the question had been adjudicated in the Supreme Court, the decisions have consistently held that *concerted efforts* to enforce a policy of standard prices for the resale of merchandise by dealers, whose property the goods are, contravene the anti-trust laws. It was so held under the Sherman Act on the ground that there was no distinction, in effect, between an arrangement whereby a manufacturer bound a great number of dealers to observe a uniform sales price and a contract by which the dealers might mutually bind each other to sell the same goods only at a price agreed upon.<sup>2</sup> In the leading case of *Miles Medical Co. v. Park & Sons Co.*, the complainant sought to enjoin the respondent, which was a large distributing organization in the drug trade, from inducing other dealers to supply them at cut prices with the patent medicines produced by the complainant, in violation of the resale covenants of contracts into which the complainant had entered with all of its recognized distributors. In denying the relief sought, the Supreme Court declared: "If there be an advantage to a manufacturer in the maintenance of fixed resale prices, the question

<sup>1</sup> See, for example, *Edison Phonograph Co. v. Kauffman*, 105 Fed. 960 (1901); *Victor Talking Machine Co. v. The Fair*, 123 Fed. 424 (1903); *National Phonograph Co. v. Schlegel*, 128 Fed. 733 (1904). It need hardly be pointed out that in all of these cases the restrictions upon resale price were imposed under patent licenses and were upheld as within the exclusive rights granted by letters patent.

<sup>2</sup> *Miles Medical Co. v. Park & Sons Co.*, 220 U. S. 373 (1911).

remains whether it is one which he is entitled to secure by agreements restricting the freedom of trade on the part of dealers who own what they sell. As to this, the complainant can fare no better with its plan of identical contracts than could the dealers themselves if they formed a combination and endeavored to establish the same restrictions, by agreement with each other. If the immediate advantage they would thus obtain would not be sufficient to sustain such a direct agreement, the asserted ulterior benefit to the complainant cannot be regarded as sufficient to support its system.<sup>1</sup>

The Supreme Court has rigorously adhered to this position in respect to contractual engagements and restrictions concerning resale price under patent or copyright licenses.<sup>2</sup> There was a persistent feeling for some years, even in the legal profession, that the exclusive rights conferred by patents might somehow operate to distinguish attempts to control the resale price of patented articles from like schemes to standardize the price of ordinary merchandise.<sup>3</sup> This misconception was finally dissolved by the blunt declaration of the Supreme Court in the *Boston Stores* case that:

“There can be no doubt that the alleged price-fixing contract disclosed in the certificate was contrary to the general law and void. There can be equally no doubt that the power to make it in derogation of the general law was not within the

<sup>1</sup> *Ibid.*, pp. 407, 408.

<sup>2</sup> See *Bobbs-Merrill Co. v. Straus*, 210 U. S. 339 (1908). Holding that a notice printed upon the cover of a copyrighted book stating the standard resale price authorized by the holder of the copyright imposed no legal restrictions upon dealers. *Bauer v. O'Donnell*, 229 U. S. 1 (1913). Holding unenforceable a notice of price restriction printed upon the package of a patented remedy, even when the contract of sale purported to be only a “license to use” the article in question. *Straus v. American Publishers' Assn.*, 231 U. S. 222 (1913). Holding illegal a combination of publishers to stop sales to distributors declining to observe the fixed resale prices which each adopted for their respective publications. *Straus v. Victor Co.*, 243 U. S. 490 (1917). Holding a comprehensive and ingenious system of “License Contracts” for distribution of plaintiff's patented musical instruments, with purported reservation of title and so-called royalty payments in lieu of purchase price, invalid as a limitation upon dealers.

*Boston Stores Co. v. American Graphophone Co.*, 246 U. S. 8 (1917). Reaffirming the principle that a manufacturer having parted with title to his product, even though patented, cannot by contract or otherwise qualify the right of the buyer to dispose of it upon terms satisfactory to himself.

<sup>3</sup> G. H. Montague, “Business Competition and the Law,” New York, 1917, pp. 141-148; A. J. Peaslee, “The Effect of the Federal Anti-Trust Laws on Commerce in Patented and Copyrighted Articles,” 28 *Harvard Law Review* (1915), pp. 394, 406.

monopoly conferred by the patent law. . . ."<sup>1</sup> As the essence of the illegality of resale price maintenance programs under the Sherman Act consisted in the drawing of merchants into an *agreement* not to sell for less than a fixed price, the question remained, however, whether it was an offense for a manufacturer merely to decline to deal with distributors pursuing the policy of selling his products for less than the price announced by him. This was settled in the Colgate case, when the Supreme Court gave judgment for the defendant upon an indictment charging violation of the Sherman Act by pursuit of the policy of refusing to sell to dealers who did not maintain the "requested" prices which it circulated to the trade.<sup>2</sup> This, at any rate, was the construction placed upon the indictment by the Supreme Court, and, so viewing it, the Court was unanimously of the opinion that no offense was charged.

The decision appears to be good law, if one accepts the interpretation of the indictment as given. A contrary rule would not only destroy that freedom of trade which it is the purpose of the anti-trust laws to protect, but would, also, be practically unenforcible. As the Supreme Court said: "In the absence of any purpose to create or maintain a monopoly, the act does not restrict the long recognized right of trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal. And, of course, he may announce in advance the circumstances under which he will refuse to sell."<sup>3</sup>

This case has sometimes been interpreted as being logically inconsistent with the earlier resale price maintenance cases.<sup>4</sup> In practical effect, it is said, the law was rendered self-contradictory. It sanctions resale price maintenance when pursued by one method and condemns it when pursued by another. If the policy is wrong under some circumstances, is it not wrong under all circumstances, it is asked. But there is nothing unusual in such a rule of law, even if it may appear illogical. As an individual, manufacturer A has the undoubted right to curtail production in his factory whenever

<sup>1</sup> 246 U. S., 25.

<sup>2</sup> 250 U. S. 300 (1919).

<sup>3</sup> *Ibid.*, p. 307.

<sup>4</sup> See, e. g., Note, 33 *Harvard Law Review* (1920), pp. 966-968.



he deems it in his interest to do so. But it does not follow that A in conjunction with B and C, his competitors, may agree each to limit his output according to a prescribed plan. The truth is the law adjusts itself to the facts, not to logic. And the facts have seemed to require the suppression, in the public interest, of concerted agreements or understandings with distributors to maintain fixed prices, whereas, in the view of the courts, the mere exercise of the private right of refusal to deal with obnoxious parties does not threaten to become an effective means of achieving standardized resale prices. That this view has some warrant in fact may be indicated by the strenuous efforts which have continued without interruption since the Colgate decision to secure an enlargement of the very circumscribed privilege which was there recognized.<sup>1</sup>

Upon repeated occasions in recent years the Supreme Court has been presented the opportunity to modify the position adopted in the leading case of the Miles Medical Company, under the mistaken assumption that the Colgate case indicated some relenting in the opposition to the practice in the form originally forbidden.<sup>2</sup> But there has been no deviation from the settled rule. As was pointedly remarked in the Schrader case: "It seems unnecessary to dwell upon the obvious difference between the situation presented when a manufacturer merely indicates his wishes concerning prices and declines further dealings with all who fail to observe them, and one where he enters into agreements—whether express or implied from a course of dealing or other circumstance—with all customers which undertake to bind them to observe fixed resale prices."<sup>3</sup> In spite of the fact, moreover, that in the Beech-Nut case the proceedings were instituted under Section 5 of the Trade Commission Act, the Supreme Court adhered to the principle that there must be some element of agree-

<sup>1</sup> An organization known as the American Fair Trade League has for a number of years been engaged in an active campaign to secure the passage of federal legislation sanctioning the practice of resale price maintenance. Among the numerous bills which have been introduced to this end may be mentioned the Stevens Bill (H. R. 13305), 63d Congress, 2d Session; the Stevens-Ashurst Bill (H. R. 13568), 64th Congress, 1st Session; and the Merritt Bill (H. R. 6), 68th Congress, 1st Session.

<sup>2</sup> *U. S. v. Schrader's Son, Inc.*, 252 U. S. 85 (1920); *Frey & Son v. Cudahy Packing Co.*, 256 U. S. 208 (1921); *Federal Trade Commission v. Beech-Nut Co.*, 257 U. S. 441 (1922).

<sup>3</sup> *Op. cit.*, p. 99.

ment, understanding, or cooperation between a manufacturer and the distributors in order to bring this price policy under the ban of the law.<sup>1</sup>

Notwithstanding these considerations the Federal Trade Commission insisted strenuously in the Beech-Nut case upon the absolute illegality of the resale price maintenance policy by whatever method pursued. This stand was based upon the admitted inconsequence of the element of contract, conspiracy, or agreement in some offenses under Section 5 of the Trade Commission Act. But the demand for such a rule involves a fundamental misconception of the nature of the objections to resale price maintenance under certain conditions. There is nothing wrongful *per se* in the conduct of a manufacturer endeavoring to establish uniform prices to consumers of his products. No unfairness toward anyone with whom he may be actually or potentially in competition can possibly result, as has already been shown. The offense, if offense there be, on his part is no more than that of being an accessory before the fact. The primary, if not the sole, objection to resale price maintenance is that it may tend, though perhaps indirectly, to restrain trade in the channels of distribution. In refusing to follow the lead of the Commission, therefore, the Court exhibited a clear understanding of the essential elements of the offense of resale price maintenance<sup>2</sup> under the settled principles of anti-trust law.

Prior to the review of the Commission's order in the Beech-Nut case, vigorous action had been taken by the Commission, on the basis of its interpretation of Section 5 of

<sup>1</sup> *Op. cit.*, pp. 453, 455. In this case the findings of the Commission, accepted by the Court, disclosed that respondent had employed every practicable means short of a written contract to enforce its so-called Beech-Nut Policy. It requested, in circulars, observance of indicated prices and announced its intention to refuse to sell to dealers not complying therewith. It requested and accepted the cooperation of dealers in keeping its goods out of the hands of price-cutters. It asked and acted upon complaints from dealers of price-cutting by other dealers. Upon assurances of willingness to comply with the Beech-Nut Policy offending dealers were restored to its list of "selected" or "desirable" dealers. Its salesmen were also charged to cooperate in carrying out this "Policy."

"From this course of conduct," runs the opinion, "a court may infer, indeed cannot escape the conclusion, that competition among retail distributors is practically suppressed. . . . The specific facts found show suppression of the freedom of competition by methods in which the company secures the cooperation of its distributors and customers, which are quite as effective as agreements express or implied intended to accomplish the same purpose." *Ibid.*, p. 455.

<sup>2</sup> See quotation in preceding footnote.

its organic act, for the suppression of the practice of maintaining fixed resale prices. In 1918, some 20 complaints had been issued against this practice, the number increasing to 32 in 1919. In 1920, there were 16 complaints in which this was the major charge, but in 1921 only 4 complaints were issued, the falling off evidently reflecting some hesitation of the Commission pending the final outcome of the Beech-Nut case. Proceedings in many of these cases reaching back even to 1918 were suspended during the progress of the Beech-Nut proceedings to final determination. Only a single order to cease and desist from the practice was issued in 1918, nine in 1919, and one each in 1920 and 1921.

Immediately that the judgment of the Supreme Court in the Beech-Nut case had finally settled the essentials of the offense, orders of dismissal were entered in some 38 cases involving resale price maintenance.<sup>1</sup> In many of these instances the complaint had been drawn upon the theory that the mere announcement of recommended resale prices and refusal to sell to parties not following these prices constituted an unfair method of competition, as tending to restrain trade. For these cases there was plainly no longer any legal foundation; and in other cases the lapse of time had vitally altered the situation. The dismissal of these complaints "without prejudice to the commencement of another proceeding by the Commission" against the particular respondents was, therefore, clearly in the public interest. The course taken by the Commission in dealing with the practice of resale price maintenance in these years, when the relation of Section 5 to this particular business policy was a matter of speculation, was in every way creditable to the Commission.

In recent years the number of complaints has again been increasing. During 1923 some 37 firms were cited for alleged violation of the rule against resale price maintenance as developed in the Beech-Nut case; and in 1924, 22 such complaints were issued.<sup>2</sup> The delays attending the Federal

<sup>1</sup> Annual Report, 1922, pp. 164, *et seq.* See, also, 5 F. T. C. 482-486.

<sup>2</sup> The products represented in the complaints against this practice are most diverse. No classification suggests itself. They range from alarm clocks, razor strops, safety razors, soaps, underwear, and breakfast foods to vacuum cleaners, cream separators, pipe threading machines, and automobile accessories. Perhaps the most frequent occasions for complaint have been in the tobacco trade; but toilet articles and coffee are represented by numerous complaints, also.

Trade Commission's procedure are nowhere better exhibited than in this class of cases, however. Of this total of 59 complaints issued in the two-year period ending June 30, 1924, only 15 had been finally disposed of up to March 1, 1925. Ten of these 15 orders directed the dismissal of the proceedings. That this record reflects an increased burden imposed upon the prosecuting agency undertaking the regulation of the resale price maintenance policy under the ruling of the Supreme Court in the Beech-Nut case can scarcely be doubted. And it suggests the query whether a more logical and practicable division of functions between the Federal Trade Commission and the Department of Justice would not lead to the transfer of this class of cases to the latter. This would be but to recognize the essential basis in the Sherman Act for proceedings of this nature. It need not involve the complete abandonment of the Commission's supervisory and investigational powers in this respect, for whenever evidence of this practice in an illegal manner came to the attention of the Commission it could be promptly reported, with recommendations, to the Attorney General. Not only would a lightening of the Commission's responsibilities in this way tend to expedite its disposition of causes, but it would have the advantage of centering the responsibility for the enforcement of the legislative prohibition of "contracts, combinations, . . . and conspiracies in restraint of trade" in one body. There is no reason why practices which are not really "methods of competition" but are "methods of combination" should not in every instance be prosecuted as violations of the Sherman Act. It is with the provisions of this law, if of any law, that resale price maintenance in its essential nature is in conflict. To the Department of Justice might well be given, therefore, the task of conducting this class of cases.<sup>1</sup>

#### §5. BASING POINT PRICE SYSTEM

The practice of quoting prices on a common center, or basing point, whether for the output of scattered plants of one concern or for the products of several independent producers located at different points, does not appear to be

<sup>1</sup>See p. 220.

widely followed.<sup>1</sup> The Federal Trade Commission has undertaken its regulation in only one industry, and in that instance the complaint was directed against one concern, the United States Steel Corporation, although it was found that independent steel producers followed the same policy.<sup>2</sup> There is nothing peculiar in the practice which would confine it to the steel industry, however, and there may be some advantage in exposition if the analysis of its economic characteristics is presented in general terms.

When a commodity is economically producible at a number of scattered points, the output from the different sources tends to be sold in separate geographical market areas. The center of each market area is roughly the most advantageous production point in the region and the bounds of the several market areas are determined by a combination of the relative costs of production and the relative costs of transportation from these centers to outlying consuming points. These two factors, moreover, determine the rise of new centers of production and new geographical market areas, but it is clear that in some instances the light weight and small volume of the product may make the transportation factor, i. e., freight, of negligible significance. Under such circumstances production for a wide, perhaps a national, market tends to become "localized" in the center of the region having the best combination of advantages for low production costs. But in the case of heavy, bulky commodities the increase of final cost to buyers with every increase in the distance from the point of production operates in favor of the multiplication of production centers and corresponding restriction of the geographical market area tributary to each. It is obvious that a new center of production for a given commodity will tend to spring up at any point where the physical factors permit its production at a cost which is

<sup>1</sup> Recent Sherman Act prosecutions have revealed the existence of a multiple basing-point system in the cement industry (*Cement Manufacturers' Protective Assn. v. U. S.*, Docket No. 551, Supreme Court, October Term, 1924. Decided June 1, 1925), and a simple basing point system in a section of the lumber industry (*Maple Flooring Manufacturers' Assn. v. U. S.*, Docket No. 342, Supreme Court, October Term, 1924. Decided June 1, 1925).

<sup>2</sup> Complaint No. 760, *United States Steel Corporation (and subsidiaries)*, Annual Report, 1921, p. 143. An order to cease and desist was issued July 21, 1924. Advance Sheets, July 23, 1924.

below the combined cost of production and cost of freight from the existing production center nearest that point.<sup>1</sup> Obversely, no competitive centers of production will ordinarily be established within the market area supplied from an existing point of production unless the output from the new source can be produced at a cost which will enable it to be sold, at least at the point of production, at a price somewhat below the delivered price of the products coming from the established source.<sup>2</sup>

For heavy, bulky commodities produced in scattered centers of production, therefore, it is plain that the normal condition of the market would show various base prices, or f. o. b. prices, at the different points of production, the variation reflecting unequal costs of production in the several regions. From these centers the delivered prices to buyers in outlying localities would tend to mount in every direction, but irregularly, on account (a) of varying pressure on different sides from the competition of other production centers, (b) of the irrational character of the railroad rate structure. Price-wise the national market would present the aspect of a number of irregularly shaped bowls placed upright on a plane surface with their rims chipped off on some sides so as to leave no uncovered space. The base of each bowl would represent the f. o. b. price, or the price of goods for local delivery, at an actual center of production. In proportion approximately to the relative elevation (or depth) of the base of each bowl would be the relative expanse of its sides. The representation would be true, of course, only for a given moment, for the prices would be constantly oscillating in response to innumerable forces affecting the demand and the conditions of production in all parts of the country.

The price situation would be quite otherwise, if a simple basing point price policy were followed.<sup>3</sup> Under such a sys-

<sup>1</sup> See, Frank A. Fetter, "The Economic Law of Market Areas," *Quarterly Journal of Economics*, 1924, Vol. 48, pp. 520-529.

<sup>2</sup> Practically, in any industry in which production costs are considerably lower for units operating on a large scale, the advantage in sales at the new point of production must ordinarily be more than this. It must be sufficient to enable something more than a mere local demand to be reached. In strict logic, however, this is covered by the formulation in the text.

<sup>3</sup> As mentioned at the outset, it is immaterial in this connection whether one has in mind the price policy adopted by a single producer to cover the output of scattered plants or the price policy adopted by several producers in different locations.

tem all parts of the current supply, from whatever geographical source, are offered for delivery at any consuming point at a price computed from the announced or prevailing base price plus the freight from some arbitrary point. The price structure, in other words, might be represented as a single bowl, of which the lowest point on its concave surface would represent the base price and of which the periphery would represent the prices at the boundaries of the geographical market. The basing point is described as an arbitrary point, since the ultimate prices computed on this basis clearly have no necessary connection with the costs of manufacture and delivery of the goods from any production center. The basing point can have no necessary connection with any particular production center, because there is no reason for more than one production center to develop unless certain consuming points can be more economically supplied from one source than from another. To quote prices for delivery at every point in the country, therefore, as though the entire supply might be economically furnished by a single production center, is to contradict the facts. This contradiction could hardly be more pronounced if, for example, the geographical center, rather than one production center, of the industry were made the common basing point, and conceivably it might be less. If one point of production is, nevertheless, adopted as a basing point for reckoning delivered prices, then there is bound to be something arbitrary in the relation of the delivered prices at different consuming points. This result cannot be avoided, for there is no conceivable reason, based upon grounds of economy, why two buyers equidistant (in respect to freight charges) from a given point of production should not, at the same time, be able to secure supplies of the same product at a uniform price. But under the basing point system a buyer situated relatively remotely from the common basing point is constrained to pay a higher price for the same product than a buyer situated at a shorter distance from the basing point, *even though the former may actually be nearer the point of production which supplies them both.*

Under such circumstances it follows that arbitrary discrimination in prices among buyers in different localities is an

inevitable accompaniment of a basing point price policy. It is equally clear that price discrimination of this kind, as of any kind, cannot exist under free competition. It would be to the competitive interest of every producer to sell to the buyers being quoted a discriminatively high price under this system, and the increasing supply competitively offered to these buyers would tend to force down the prices at such consuming points. This tendency would eventually lead to the equalization of the price realized by the producer for all portions of the current output of each plant, and whatever differences in prices paid by ultimate buyers anywhere persisted would reflect differences in the costs of production in different regions and in the costs of transportation to the points of delivery actually required. In short, the price situation might again be represented by a number of irregularly shaped bowls.

From the standpoint of public policy, it may be concluded, the practice of quoting prices upon a common basing point in an industry in which production is carried on in widely scattered centers may be considered subject to regulation on two grounds: First, the practice under the given circumstances is evidence of monopolistic control of the supply of the commodity the prices of which are thus quoted. The practice involves arbitrary discrimination among buyers, and that is an infallible sign of monopoly.<sup>1</sup> Secondly, the practice under the given circumstances is unfair to the buyers. It is unfair not only because of the monopolistic element in the prices which result from its operation, but also because arbitrary discrimination is willful discrimination and willful discrimination subjects buyers to the risk of unpredictable contingencies. Particularly under conditions in which the buyers are not ultimate consumers, but are engaged in further processes of manufacture, the unfairness resulting from the arbitrariness of prices under the basing point system is inimical to enterprise.<sup>2</sup>

<sup>1</sup> Monopoly, as the term is here used, need not denote financial and legal unity. Agreement, understanding, or mere mutual forbearance among a group of sellers might suffice to accomplish the discrimination.

<sup>2</sup> Though the discrimination may well constitute a special safeguard to particular manufacturer-buyers, on account of the dependence of the price structure on the caprice of benevolently disposed interests.



Both these reasons seem to have influenced the Federal Trade Commission in its condemnation of the so-called Pittsburgh Plus system in the steel industry.<sup>1</sup> In the sale of semi-finished rolled steel products Pittsburgh was used as a basing point for quoting prices to any point of delivery in the United States, regardless of whether the steel was to be supplied from Pittsburgh, Chicago, Duluth, Birmingham, Pueblo (Colorado) or Sparrows Point (Maryland). The Steel Corporation or its subsidiaries operated mills in only the first four of these districts, but for certain forms of rolled steel it appeared that the Pittsburgh Plus policy was followed by substantially all producers.<sup>2</sup> The system was neither universal nor symmetrical, however. In the Chicago district, for example, plates, shapes and bars were exempted from the common basing point price policy in 1921, after the proceedings had been commenced.<sup>3</sup> And Southern steel users had earlier been successful in agitating for a modification of the system, which resulted in the establishment of a supplementary Birmingham base with a fixed differential, somewhat less than the Pittsburgh-Birmingham freight rate, above the Pittsburgh base.<sup>4</sup> Nevertheless, the Pittsburgh Plus system was found, as it was actually operated, to embody the arbitrary, unfair, and discriminatory characteristics which have been shown to pertain to a common basing point price policy in an industry of this type. Accordingly, the Commission, after an extensive investigation and prolonged hearings, ordered the respondents to cease and desist from the practice of quoting or selling their rolled steel products "upon any other basing point than that where the products are manufactured or from which they are shipped."<sup>5</sup>

While objections to the specific wording of the order might have been raised on the ground of the inelasticity it introduces into business practice, the United States Steel Corpora-

<sup>1</sup> See Annual Report, 1924, pp. 36-40.

<sup>2</sup> Upon these special features of the case, consult the Findings as to the Facts as reported in the Advance Sheets (F. T. C.) July 21, 1924. Cf., particularly, p. 22. See, also, for a full discussion of the practice, John R. Commons, "Delivered Price Practice in the Steel Market," *American Economic Review* (1924), Vol. XIV, pp. 505-520.

<sup>3</sup> Advance Sheets, *op. cit.*, Paragraph 14, p. 26.

<sup>4</sup> Advance Sheets, *op. cit.*, Paragraph 18, p. 31.

<sup>5</sup> Advance Sheets, *op. cit.*, Order to Cease and Desist, Paragraph 2, p. 2.

tion announced on September 17, 1924, its intention to comply with the terms of the order as issued. The chief criticism of the ruling, founded on the dissenting opinion of Commissioner Gaskill, has been of its failure to reach the primary source of the discrimination which the Commission found to have resulted from the use of the Pittsburgh Plus system. In effect, a method of determining price quotations found to be discriminatory was condemned, it is said, but the power which enabled discriminatory prices to be enforced was left untouched.<sup>1</sup> However that may be, the scope of the instant proceedings was limited by the jurisdiction of the Commission under Section 5 of its organic act and Section 2 of the Clayton Act, and it cannot be doubted that the terms of the order were influenced by the favorable judgment of the Supreme Court four years earlier in the prosecution under the Sherman Act.<sup>2</sup>

Upon the final effects of the abandonment of the Pittsburgh Plus system it does not seem necessary here to speculate. The trepidation in the trade attending the announcement of its abandonment seems to have disappeared, and the ultimate adjustments which will have to be made will in any event depend upon the extent of the modification in the Corporation's price policy. But some steel fabricators, i. e., buyers of rolled steel products, who by virtue of their location enjoyed special advantages under the Pittsburgh Plus system, appear to be experiencing difficulties in the new situation.<sup>3</sup> That this was no more than to have been expected from the abandonment of a basing point price policy has already been shown.

#### §6. GUARANTEE AGAINST PRICE DECLINE

Though it appears the price guarantee policy has been followed for a long time in some lines of trade,<sup>4</sup> it became a

<sup>1</sup> See p. II of Memorandum of Dissent, in *Advanced Sheets*, July 23, 1924.

<sup>2</sup> *U. S. v. United States Steel Corporation*, 251 U. S. 417 (1920).

<sup>3</sup> See, e. g., E. C. Kreutzberg, "The Passing of Pittsburgh Plus," *American Bankers' Association Journal* (1924), Vol. 17, p. 301. The writer seems to feel that there is an element of unfairness to these fabricators in the present policy of basing prices on the points of production. The basis of the argument appears to be that these favored fabricators acquired some sort of a vested interest in the Pittsburgh Plus system.

<sup>4</sup> E. g., in the hardware trade and in the distribution of sugar.

wide-spread practice only in the post-war period of fevered trade activity.<sup>1</sup> At that time the uncertainty in the business world with respect to the future course of prices was so great and yet the immediate demand for goods so urgent that manufacturers sought some means of spreading out the flood of prompt shipment orders into orders for future delivery.<sup>2</sup> They found the policy of offering to assume the risks of a decline in prices the most effective device for overcoming dealer-resistance to future commitments. Originally, in its typical form, the guarantee against price decline was simply an agreement by a manufacturer to protect a distributor against a fall in price between the date of order and the date of delivery. It amounted to a contract of indemnity to the buyer against a price reduction during manufacture and shipment.

This practice, once started, spread rapidly since competitors were obliged to adopt it in self-defense. Moreover, it was soon extending itself on another plane. If manufacturers were willing to take the risk of price-changes, under a binding sales contract, up to the time of delivery of the goods, why should they not also agree to carry the burden up to the date of settlement or even beyond? The dealers were not averse to this shifting of responsibility for the anticipation of demand, and under stress of competition many manufacturers extended the guarantee to cover a specified period following delivery to the dealer. The unfortunate results of this liberality in throwing the losses from a slackening of demand directly back upon the shoulders of the manufacturers, uncushioned by any intermediate "shock-absorbers," were demonstrated in 1921. But while this experience led to the abandonment of the policy by many manufacturers strong enough in their sales position to resist the dealer demand for price protection, there are numerous lines of trade in which the practice continues.

In these circumstances, are there valid grounds for regu-

<sup>1</sup> See, "Digest of Replies in Response to an Inquiry of the Federal Trade Commission Relative to the Practice of Giving Guarantee against Price Decline," Washington, May 27, 1920.

<sup>2</sup> In the hysteria of the 1919-20 boom, dealers in many lines ordered goods far in excess of their anticipated requirements in order to secure preference in deliveries and the manufacturers, having already reached capacity production, were forced to prorrate orders. This, of course, led to still further inflation of orders and so on in a vicious spiral.

lation of the price guarantee policy by the Federal Trade Commission? As no question of discrimination among buyers is presented, the problem resolves itself into the applicability of the prohibition of unfair methods of competition. That there is nothing immoral or opposed to business ethics in the practice will not be disputed. But it has been alleged that such a price policy is uneconomic from the social point of view and may, therefore, be treated as contrary to public policy. This seems to have been the view of the Commission itself for a time and during 1919 some eleven complaints were issued charging individual manufacturers with violation of Section 5 on account of the use of this policy.<sup>1</sup> Since then all of these cases have been dropped, and though the formal notices of dismissal in some of the earlier decisions were not very specific,<sup>2</sup> the Commission has lately stated expressly that "the practice of guaranteeing the price of a commodity against decline is not in and of itself an unfair method of competition within the intent and meaning of the Federal Trade Commission Act."<sup>3</sup>

It might appear, in view of this changed attitude of the Commission, that the discussion of the amenability of this particular variety of price policy to federal regulation was no longer appropriate. But the vigorous dissent of two of the Commissioners to these orders of dismissal, considered in connection with changes in administrative personnel, justify some analysis of the economic consequences of price guarantees.

The essence of the policy of a manufacturer in guarantee-

<sup>1</sup> The first of these complaints was issued in December, 1918, the remainder in 1919:

- Complaint No. 227 *Helvetia Milk Condensing Co.*
- Complaint No. 424 *Lantz Bros. & Co.*
- Complaint No. 425 *Fels & Co.*
- Complaint No. 426 *Globe Soap Co.*
- Complaint No. 427 *B. T. Babbitt.*
- Complaint No. 428 *Curvice Bros. Co.*
- Complaint No. 429 *Joseph Campbell Co.*
- Complaint No. 445 *Louisville Soap Co.*
- Complaint No. 446 *Van Camp Packing Co.*
- Complaint No. 520 *Proctor & Gamble Distributing Co.*
- Complaint No. 522 *Rub-No-More Co.*

<sup>2</sup> Complaint No. 227, against the *Helvetia Milk Condensing Co.*, is simply reported as "Dismissed without prejudice." See Annual Report, 1923, p. 213.

<sup>3</sup> Advance Sheets, February 6, 1925, announcing dismissal of Complaints No. 245, 426 and 522 against the following soap manufacturers, respectively: *Fels & Co.*, *Globe Soap Co.*, and *Rub-No-More Co.*

ing distributors against price declines is to accomplish a transfer of risks. The sole question that it raises is whether the manufacturer is in a better position to foresee the trend of demand and the consequent trend of prices and, therefore, to minimize the hazard by regulating the supply than is the merchant. There are those who contend that the merchant is a specialist in interpreting demand and that, impelled by the risk of loss on goods ordered, he will find means of discharging this function more efficiently than the manufacturer, already occupied with problems of productive efficiency. Deprived of the check which the risk of a fall in prices places upon his judgment in ordering goods, however, the merchant will be prone to "over-buy" on a rising market, it is said, and make the convulsions of depression in trade, when they arrive, all the more severe. There are others who point to the superior vantage point of a manufacturer, in touch with all parts of a wide market, for the purpose of forecasting the movement of prices. With the responsibility of compensating dealers for losses by price declines upon goods in their hands, or being manufactured for their order, he will be compelled to utilize his superior advantages to stabilize business in two ways, it is contended. First, he will have an interest in scrutinizing orders of dealers and withholding the guarantee upon goods sold in excess of the volume which in his judgment will find ultimate purchasers at profitable prices. Secondly, he will have an interest in not precipitately forcing goods upon the market at great price concessions, demoralizing if not disastrous to distributive trade, when the withdrawal of demand does occur. For these reasons business is thought to become more stable under price guarantees.

Which of these arguments represents the sounder analysis, if indeed each might not prove to be valid in different lines of trade,<sup>1</sup> there is no occasion here to decide. For this is manifestly a question which cannot be satisfactorily answered by bureaucratic fiat or solved by scholarly disquisition. There is no reliable way to reach a decision regarding the respective capacity of manufacturers and merchants to assume market-

<sup>1</sup> In seasonal industries the advantage of securing advance orders is perhaps most pronounced and the assumption of part of the marketing risks by producers in these industries might, therefore, be especially warranted. It would tend to keep down manufacturing costs.

ing risks other than by the test of experience. No better method of determining the most economical division of functions among successive agencies in the economic process has been discovered than by "trial and error." There seems not the slightest ground to doubt that if manufacturers in a given industry cannot anticipate demand and price changes more accurately than distributors, those manufacturers who adopt the policy of guaranteeing buyers against price declines will be handicapped in competition. And under these circumstances the practice may be counted upon to disappear. If the results prove otherwise, the spread of the practice may be looked for, and in that event it will be unfair to no one.

In conclusion, it may be noted that the Federal Trade Commission has latterly issued several complaints against trade associations of dealers for exerting collective pressure upon manufacturers to force the adoption of the price guarantee policy.<sup>1</sup> This presents quite a different issue from the direct attack upon the pursuit of the practice. A trade boycott is a peculiarly potent instrument of coercion. In its very essence, i. e., without regard to the particular object for which it is organized, it interferes with the competitive rendering of trade or market adjustments. Used for compelling manufacturers to grant their customers guarantees against price declines, it may not properly be regarded as an "unfair method of competition," since the producers and the distributors are not strictly speaking in competition, but it is nevertheless vicious and unlawful beyond doubt under the Sherman Act. The Federal Trade Commission, however, under the elastic interpretation of Section 5 already referred to, has issued orders to cease and desist in two of these instances in which prosecution under the Sherman Act would have been the more logical procedure.<sup>2</sup>

<sup>1</sup> Complaint No. 893, *St. Louis Wholesale Grocers' Assn.*, 7 F. T. C. 1 (1923).

Complaint No. 894, *Wisconsin Wholesale Grocers' Assn.*, Annual Report, 1922, p. 140. Order issued May 23, 1924.

Complaint No. 922, *Michigan Wholesale Grocers' Assn.*, Annual Report, 1923, p. 182. Dismissal announced May 11, 1925.

Complaint No. 952, *Penna., N. J., and Del. Wholesale Grocers' Assn.*, Annual Report, 1923, p. 186. Dismissed February 13, 1925.

Complaint No. 957, *Ohio Wholesale Grocers' Assn. Co.*, Annual Report, 1923, p. 186. Dismissed May 28, 1925.

<sup>2</sup> *St. Louis Wholesale Grocers' Assn.*, *op. cit.* *Wisconsin Wholesale Grocers' Assn.*, *op. cit.*

## CHAPTER V

### THE REGULATION OF SALES PROMOTION POLICIES

#### §1. INTRODUCTION

It is in the cultivation of sales that the enterprise and ingenuity of business managers are most strikingly revealed. No general circumscription of the methods of sales promotion could, in the nature of things, be established without radically impairing one of the most vital phases of the competitive process. It would stereotype business practice and deprive it of that elasticity and that experimental quality which may be counted among the saving graces of the capitalistic régime. If, upon the ground of experience, the private management of industry and commerce is to be sanctioned, there is coordinate reason for maintaining a wide scope for both technical and administrative initiative. Only thus can the distinctive fruits of the system of free enterprise be assured.

But it does not follow that no limitations upon methods of salesmanship are warrantable for the protection of the buying public and the preservation of fair competitive opportunity. Some specific types of selling activity are flagrantly opposed to the common principles regulating ordinary human intercourse, and those who indulge in them are able to play upon the credulity of a wide section of the public. In issuing, so to speak, their irredeemable drafts upon the scanty fund of social trustfulness, these charlatans of trade may secure large immediate returns from their operations, but they undermine the credit<sup>1</sup> (good-will) of honest traders along with their own, at the same time they are exploiting the buyers. Those business managers who are callous enough to take advantage of the public confidence resting upon an implicit respect for the rules of common morality are, therefore, subject to restraint,

<sup>1</sup> The reference here is, of course, not to financial credit, i. e., borrowing power, but the general confidence of consumers in business institutions.

but their selling policies still are regulated only in so far as they involve a breach of the most elementary precepts of fair dealing. Neither legal rules nor economic principles require the utmost candor and the strictest veracity of traders in soliciting custom. But even under the relatively simple economic conditions in which the common law grew up it was found indispensable to provide safeguards against the grosser forms of fraud, as has previously been shown. Under the complex and unstable conditions characterizing the modern market it is patent that the same considerations of social expediency dictate an extension of the prohibitions embodied in the technical doctrine of fraud if the relative degree of protection to the general public is not to be relaxed.

In precisely what measure the actual situation enjoins a curb upon the private discretion of business management in the selection of selling methods it is impossible to state categorically. It is one of those problems in the solution of which judgment plays a larger part than logic. And where distinctions of degree are uppermost, complete agreement upon the elements of sound policy is not to be expected. Still it should be possible to formulate the standards according to which the lines of policy may be drawn to general satisfaction. The basic standard, under existing circumstances, may be taken as the preservation of fair competitive opportunity in trade.<sup>1</sup> Selling policies or tactics which tend to preclude rival producers from attracting such custom as their goods could win on their merits may be deemed unfair no less than uneconomic. This, of course, represents only an abstract standard, but it provides nevertheless a more definite test of the soundness of specific regulations of selling methods than such a standard as the protection of the long-run interests of the consuming public. That familiar principle, while admissible in theory, is quite too vague for practical usefulness. And it is clear that neither social tradition,

<sup>1</sup> Support for this view may be found in the opinion of the Supreme Court in the leading case of *Federal Trade Commission v. Winsted Hosiery Co.*, 258 U. S. 483 (1922). The Court declared: "As a substantial part of the public was still misled by the use of the labels which the Winsted Company employed, the public had an interest in stopping the practice as wrongful; and since the business of its trade rivals who marked their goods truthfully was necessarily affected by that practice, the Commission was justified in its conclusion that the practice constituted an unfair method of competition."



nor legal doctrine, nor economic analysis sanctions an extension thereof which would set up the full protection of the consumers' immediate interests in every transaction as the sole limiting principle of public regulation in this sphere. The facts afford no support for such a far-reaching retraction of the salutary tenets of self-reliance and individual responsibility underlying the whole modern polity.

If the standard of the preservation of fair competitive opportunity in trade be accepted, then, as the criterion of sound policy in the governmental regulation of methods of sales promotion, the inquiry may proceed to the consideration of the concrete record of the exercise of administrative authority in this field. The Federal Trade Commission has not formally adopted any rigid classification of the causes in which it has determined the public interest to be sufficiently at stake to warrant the issuance of complaints against "unfair methods of competition." In other words, the formal procedure of the Commission takes no account of types of unfair competition. Each given state of facts, as disclosed by preliminary investigation or by the findings of an examiner at the hearing, is treated as a distinct issue determinable only with reference to the general, and it must be added somewhat vague, conception of the scope of the legislative prohibition. Solely for convenience of reference, the Commission has furnished a digest to its reports,<sup>1</sup> but the particularity of a classification adopted for this purpose is much too great to make it serviceable for a systematic survey and analysis of the Commission's work. For the present purpose, that part of the regulative activities of the Commission directed in substance at methods of sales promotion may be treated under a ten-fold classification. These divisions are: (1) misbranding, (2) misrepresentation of quality, condition or value, (3) false claims to endorsement, (4) misrepresentation of trade status, (5) misrepresentation of origin, (6) false packaging, (7) lotteries, (8) misrepresentation in sale of securities, (9) commercial bribery, (10) trade name or trademark simulation.

<sup>1</sup> This digest is, of course, in no way comparable to the ordinary legal digest attached to judicial reports, which is based upon forms of action and specific technical issues raised by the pleadings and settled by the judgment or decree of the court.

## §2. MISBRANDING

The Federal Trade Commission has been energetic in its prosecution of unfair selling practices. Of the 1,197 complaints which had been filed prior to June 30, 1924, over four hundred dealt with some form of misrepresentation.<sup>1</sup> Not only first in point of time, but also, perhaps, in point of importance to the general public, are the cases in which misbranding has been condemned. Shortly after the Federal Trade Commission was organized, representatives of the Silk Association of America directed the attention of the Commission to the fact that a number of textile firms were representing their products as being made of silk when in reality they contained not a thread of silk. Proceedings were instituted and ultimately the respondents in a number of these cases were required, by formal orders, to cease and desist from such misrepresentation.<sup>2</sup> Subsequently the Commission has issued orders to prevent similar misrepresentation in the sale of cotton goods as wool,<sup>3</sup> of celluloid as ivory,<sup>4</sup> of phosphate baking powder as cream of tartar baking powder,<sup>5</sup> of mineral oil mixtures as linseed oil,<sup>6</sup> and of various other substitutes for standard commodities.<sup>7</sup>

<sup>1</sup> This does not include some two hundred complaints directed against commercial bribery and lotteries, which also involve deception, but of a different stamp.

<sup>2</sup> For a typical case, see: *A. Theo. Abbott & Co.*, 1 F. T. C. 16 (1916). The respondent was found to have labelled a cotton product as "Kapock Silk," the information that it was "not a worm silk" being printed on the bottom of the label in minute, inconspicuous letters. "Kapock" was a registered trade name. The order directed the respondent to "forthwith cease using the word 'silk' . . . in reference to their 'Kapock' fabrics as now manufactured. . . ."

The Commission in another case condemned as deceptive and misleading the use of the word "Cilk" to describe artificial silk goods. *Circle Cilk Co.*, 1 F. T. C. 13 (1916).

<sup>3</sup> *Winsted Hosiery Co.*, 2 F. T. C. 202 (1920); *H. E. Bradford Co.*, 2 F. T. C. 207 (1920); *Daum, Rogers, Spritzer Co.*, 5 F. T. C. 257 (1922); *Sulloway Mills*, 5 F. T. C. 269 (1922). These cases are merely representative of a much larger number having substantially similar facts.

<sup>4</sup> *Palais Royal*, 4 F. T. C. 305 (1922); *Louis K. Liggett Co.*, 4 F. T. C. 423 (1922); *Peoples Drug Stores*, 4 F. T. C. 446 (1922); *Hyman & Laslow*, 6 F. T. C. 97 (1923); *Holsman Co.*, 6 F. T. C. 203 (1923); *Raff & Son*, 6 F. T. C. 462 (1923); *Atlantic Comb Works*, 7 F. T. C. 274 (1924).

<sup>5</sup> *Royal Baking Powder Co.*, 4 F. T. C. 1 (1921). This case is unique.

<sup>6</sup> *Plomo Specialty Manufacturing Co.*, 2 F. T. C. 195 (1919); *Penn Lubric Oil Co.*, 2 F. T. C. 295 (1920); *Sanitary Turpentine Co.*, 2 F. T. C. 313 (1920); *Ohio State Linseed Co.*, 2 F. T. C. 321 (1920); *Star Provision Co.*, 3 F. T. C. 393 (1921).

<sup>7</sup> *Dings & Shuster*, 6 F. T. C. 340 (1923); *Max Baer*, 6 F. T. C. 481 (1923). These cases restrained traders from describing as "shellac" varnishes which had other gums as their base.

A case perhaps as typical of the actions of this description as any was that against the Winsted Hosiery Company; and as it was made a test case and appealed to the Supreme Court it may well serve as the basis for discussion of the misbranding practice. The custom had become quite prevalent in the textile trade, and particularly in the hosiery and underwear branches, of branding or labelling goods composed in whole or in part of cotton with terms implying that they were made of wool. Among the labels in common use were those describing the garment as: "Men's Knit Merino," "Gray Wool," "Cashmere," "Worsted" and "Australian Wool." The respondent in this particular case had used several of these terms in marking and advertising its products which contained no more than a small percentage of genuine wool. The practice was of such long standing, however, that it was contended that wholesalers and retailers of these goods were not deceived thereby. The Commission found, nevertheless, that the consuming public were continually being imposed upon by the presence of these misleading labels on hosiery, underwear and other garments. It regarded this as unfair to competitors who truthfully labelled their products, and ordered the Winsted Hosiery Company to stop the practice.<sup>1</sup> The company applied to the circuit court of appeals for a review and that court reversed the Commission's order.<sup>2</sup> Upon appeal to the Supreme Court, Justice Brandeis delivered an opinion, supported by a unanimous court, fully sustaining the Commission.<sup>3</sup> To the argument that the meaning of the labels was so well known in the trade to indicate goods made at least partly of cotton that there existed no deception of dealers and therefore no injury to competing manufacturers, the Supreme Court answered that the labels were plainly deceptive to the ultimate purchasers and through this deception the injury of the makers of all-wool goods was accomplished. The Court declared that the question of unfairness was not confined to the effect of the practice on the direct competitors of the respondent making cotton hosiery and underwear, most of whom indulged in similar

<sup>1</sup> 2 F. T. C. 202 (1920).

<sup>2</sup> *Winsted Hosiery Co. v. Federal Trade Commission*, 272 Fed. 957 (1921).

<sup>3</sup> *Federal Trade Commission v. Winsted Hosiery Co.*, 258 U. S. 483 (1922).

forms of misleading branding. It was the manufacturers of genuine woolen articles of this type who suffered from a narrowing of the market for their products; and their competition with the respondent was obviously secondary or collateral—as bananas compete with oranges for the demand of fruit consumers. But the Court did not hesitate to protect this collateral competition by declaring the deceptive labelling of cotton goods an unfair method of attracting trade from the producers of alternative goods, i. e., woolen undergarments.

The significance of this important ruling can scarcely be overemphasized. It has greatly strengthened the position of the Commission in its campaign against misbranding, for it not infrequently happens, as here, that a species of misrepresentation fastens itself upon the marketing methods of an entire branch of trade so that it would be extremely difficult to prove that it injured any of the direct competitors therein. But it is sufficient, under the decision in the *Winsted* case, if the consuming public tends to be misled so that purchasing power will be diverted from one class of products to an alternative class of products. Thus, if stringent statutes had not already been passed in many states specifically prohibiting the sale of oleomargarine disguised as butter, this practice could be reached now under the Federal Trade Commission Act, even though no injury were shown to any manufacturer of oleomargarine. As such misbranding would tend simply to enlarge the sales of oleomargarine at the expense of the demand for butter, the special damage to oleomargarine producers might be difficult to establish. The scope and effectiveness of the jurisdiction of the Federal Trade Commission in the suppression of false branding, which the *Winsted* decision confirmed, have been well illustrated by a number of prosecutions in the paint and varnish industry, some of which were cited above. It has forbidden the use of the word "turpentine" to describe a coal-tar product being passed off to the public for turpentine;<sup>1</sup> and the labelling of a paint mixture which contained 98 per cent of coal tar as "graphite carbon roof paint" was also condemned.<sup>2</sup> In the

<sup>1</sup> *International Paint & Oil Co.*, 6 F. T. C. 16 (1923).

<sup>2</sup> *Montgomery Ward & Co.*, 3 F. T. C. 151 (1920).

celluloid products industry the Commission has had the active cooperation of a large part of the trade in its endeavor to prevent the sale of these products under misleading names.<sup>1</sup>

In the foregoing type of case the work of the Commission calls for no special comment. The public is undoubtedly entitled to protection from downright fraud and in most of these cases the misrepresentation has certainly bordered, at least, on that offense. But there have been some cases which raise the question of just how far administrative regulation may properly be carried in controlling the marking, labelling, or naming of privately produced commodities. In a recent case, for example, a soap manufacturer was ordered to stop using in labels or brands upon soap "the fatty ingredient of which is not composed entirely of olive oil . . . the word 'Olive' alone or in combination with any other word or words, unless accompanied by a word or words designating the constituent elements other than olive oil constituting in part the fatty ingredient of the soap."<sup>2</sup> It may be questioned whether so rigorous an order is required in the public interest.

The essential problem in such cases is as to what extent immediate or ultimate buyers of the product are deceived by the labelling adopted or the failure to make the label truthful or completely descriptive. In some cases the effective deception is more serious than in others. Purchasers of soap for domestic use, for example, may be interested only to know whether a soap labelled "Olive Oil" contains that ingredient and they may generally understand that it is not made solely of such material. In the case of a soap used industrially, however, knowledge of the exact composition may be of vital importance. If it were the common practice in an industry to use soap made entirely of olive oil, the sale to manufacturers in that industry of a soap labelled "Olive," and containing other ingredients beside, would be deceptive.<sup>3</sup>

<sup>1</sup> See Trade Practice Submitted by Pyroxlin Plastics Industry, May 20, 1920. The mode of procedure in trade practice submittals will be explained and criticized in Chapter VII.

<sup>2</sup> *Crofts & Reed Co. and Polonia Soap Co.*, 6 F. T. C. 466, 474 (1923).

<sup>3</sup> In this connection should be noted the recent dismissal of a complaint against the *Advance Paint Company* for selling a varnish labelled "Improved O'Shellac" which contained no genuine shellac gum. Complaint No. 1256. Dismissal reported May 5, 1925. The order of dismissal explains that the product was sold solely to furniture manufacturers "who understand fully that it is not composed of genuine shellac gum."

In this instance, as in the case of numerous other commodities compounded from a variety of elements,<sup>1</sup> it seems clear that the use of descriptive words in a label or brand is not intended to and does not actually convey to the consuming public, let alone to dealers, the impression that the article in question is composed entirely of the one material. On this practical ground these cases may readily be distinguished from those cases in which buyers are reasonably justified in inferring from the use of descriptive words in an unqualified sense that the article to which they are applied is a simple, homogeneous substance.<sup>2</sup> Unless such practical considerations guide the Commission in its regulation of misbranding, administrative supervision may easily become an intolerable burden. This is not to approve of misrepresentation, however slight or innocuous, in the sale of merchandise. It is only to emphasize that while the complete elimination of all species and degrees of deception in trade would be desirable, it is not feasible to undertake any such far-reaching program by administrative regulation, even if constitutional authority could be found for pursuing such an ideal by coercive means.

In conclusion, it may be emphasized that it has not been the policy of the Federal Trade Commission, as it clearly could be no part of a sound program of administrative regulation, to restrict the production and sale of substitutes for well-known commodities. The object of the Commission's activity has been only to prevent the unfair competition which results from a misrepresentation of their character, a

<sup>1</sup> For example, in *Louis Philippe, Inc., and Park & Tilford*, 5 F. T. C. 136 (1922), the respondents were charged with misrepresenting a toilet preparation, called "Creme Angelus," by advertisements stating it was "made with real lemons." The Commission, after finding that the preparation contained no lemon juice but did contain a constituent derived from lemon rind, ordered the respondents to cease and desist from advertising the product in a manner tending "to create in the minds of the purchasing public the erroneous belief that such preparations contain the juice of lemons." In view of the fact that the respondents had expressly directed their advertising agent to avoid any statements to the effect that the preparation contained lemon juice, there would seem to be meagre ground for the order to cease and desist. The misrepresentation here, if any, was so insignificant that the complaint might very properly have been dismissed, and it is encouraging to note that subsequently in a substantially identical case this was the course taken. *Friedrich-Friedrich Chemical Co., Complaint No. 1179*, Annual Report, 1924, p. 233. Dismissed August 31, 1924.

<sup>2</sup> As, for example, "linseed oil," or "woolen" garments, or "silk" goods.

deliberate confusion of their identity with that of standard and familiar articles of consumption. In endorsing the report of a conference of the pyroxylin plastics (celluloid) industry in a trade practice submittal held in 1920 the Commission announced: "The Commission does not attempt to force the members of the industry to brand or mark their goods as to quantity, quality, or substance. When, however, the members of the industry do mark or brand their goods, such marks or brands shall be so definite and correct as not to deceive the purchasing public with respect to the quantity, quality, or substance of the goods purchased."<sup>1</sup> So long as this policy is adhered to there can be no just complaint from the producers of substitute commodities. They have an unqualified right to place on the market, and in every way consistent with honest dealing to advance the sales of, imitation or substitute merchandise. The public has an interest in having new and cheaper compounds that serve essentially the same ends as traditional materials offered for their choice. But the public also has an interest in not being subtly misguided in that choice by deliberate misinformation. The expanding range of synthetic products which the ingenuity of industrial chemists is providing furnishes an increasing need for vigilant and vigorous administrative regulation to restrict the temptation to market them under the name of the genuine substance which they imitate.<sup>2</sup> The utility of these cheaper substitutes may be and often is equal to the original, but they have an initial handicap to overcome by reason of ingrained habit and conservative prejudice on the part of buyers. This affords no warrant, however, for marketing them under the name of the familiar article traditionally serving the same need. The injury to competitors from such a selling policy may be less in magnitude but is not otherwise less condemnable than in the case where the purchaser is more seriously defrauded.

<sup>1</sup> Trade Practice Submittals, November 6, 1919, to January 18, 1923, Washington, D. C., pp. 14-19. The quotation is found on p. 19. The nature of this form of procedure is discussed in Chapter VII, below.

<sup>2</sup> The number and variety of useful articles made from coal-tar derivatives alone is amazing. See "Diagram of the Products Derived from Coal . . ." prepared by The Bennett Co., New York, 1916. Cf., also, P. E. Spielmann, "Constituents of Coal Tar," London, 1924.

### §3. DECEPTIVE ADVERTISING CONCERNING QUALITY, CONDITION, OR VALUE OF GOODS

Fraudulent misrepresentation may be carried on by other practices no less effective than misbranding, and the Federal Trade Commission has not limited its endeavors to eliminate deceptive selling policies to that particular type. False and misleading statements regarding the quality or condition of the given product, as distinguished from its composition, have furnished the basis of a number of complaints. Deceptive advertising differs from misbranding in that assertions respecting the quality or usefulness of an article are less capable of exact verification than assertions regarding its component elements. How much, if any, wool is contained in underwear labelled "Australian wool" is purely a question of fact capable of exact determination. But the truth or falsity of the claim that "We are able to offer you seed which no other seed firm can secure," cannot in the nature of things be established conclusively.<sup>1</sup> A similar distinction has long been familiar to lawyers, for the common law of sales drew a sharp line between statements of fact and statements of opinion. The confusion in the courts from trying to adhere to such a line of demarcation in concrete cases is paralleled by the experience of the Commission in its attempt to regulate methods of sales promotion.

At the one extreme stand the clearly fraudulent cases in which respondents sell goods as of a certain well-established standard grade which are in truth of a lower grade. Representative of this type of cases was the proceeding against a jobber of window glass who opened the shipping boxes, changed the packing marks indicating quality, and sold a cheap grade of glass as a higher grade product.<sup>2</sup> In another case a chemical manufacturer was required to stop advertising a weak and fairly innocuous preparation as a powerful disinfectant, "ten times stronger as a germicide than undiluted U. S. P. carbolic acid."<sup>3</sup> From plain falsehoods such

<sup>1</sup> Cf. *American Mutual Seed Co.*, 3 F. T. C. 177 (1921).

<sup>2</sup> *A. T. McClure Glass Co.*, 1 F. T. C. 113 (1919).

<sup>3</sup> *Ginso Chemical Co.*, 4 F. T. C. 155 (1921). Hardly less clearly fraudulent is the advertisement of job printing work done upon an ordinary type press but with the lettering raised by a chemical process as "Relief-Engraving," or "Process Engraving." True engravings are produced by impressions from engraved plates, and



as these about the definite quality or grade of goods the cases of this general description shade off into expressions which amount to little or nothing more than extravagant praise. Thus, a manufacturer of electric storage batteries has been ordered to cease advertising that "Universal batteries last forever."<sup>1</sup>

As in the case of misbranding, the basic issue in respect to deceptive advertising in general is whether the statements made are of such a character as to deceive a substantial portion of the purchasing public to the injury of competing producers. It seems clear that, on this basis, mere exaggeration does not furnish adequate ground for interference. Objectionable as every manner of falsification may be, from the ethical standpoint, it would seem not to be the function of the Federal Trade Commission to pass upon the usual claims to superiority or excellence which constitute the soul of advertising. Upon statements regarding the actual physical properties of merchandise the consuming public is reasonably justified in relying and the Commission in its efforts to rid trade of fraud may well afford protection against this form of misrepresentation. But to forbid all "puffing" of their wares by traders and manufacturers, to attempt to establish by compulsion the standard of absolute truthfulness in advertising, would involve a species of bureaucratic paternalism which is not only inconsistent with tradition but is not required for safeguarding the legitimate interests of buyers. It is too well recognized to need argument that advertising exaggeration is common, and that such claims as "the best in the market," "will last indefinitely," and "has the most beautiful design obtainable" are wholly unreliable. Some gullible portion of the buying public may be misled by such assertions, but the administrative process of regulation is no more adapted than the judicial process to winnowing the true from the false in such matters.

Fortunately the instances in which the Federal Trade Commission appears to have overstepped the bounds of

the deception caused by this form of misrepresentation, with the consequent injury to those engaged in producing actual engravings, is obvious. See: *Turner & Porter*, 7 F. T. C. 100 (1923); *Process Engraving Co.*, 7 F. T. C. 287 (1924); *Plateless Engraving Bureau*, 7 F. T. C. 399 (1924).

<sup>1</sup> *Universal Battery Service Co.*, 2 F. T. C. 95 (1919).

judicious regulation in this class of cases are relatively rare. And it must be recognized that in practice the limits of justifiable intervention are indistinct. This may be emphasized by reference to a group of cases in the rebuilt tire trade. It is unquestionable that manufacturers are injured by the sale of second-hand goods as and for new and first class.<sup>1</sup> A process of renovation does not restore a used tire to its original condition, even though it may be a serviceable article. Accordingly, it has been held an unfair method of competition to market rebuilt tires without clear indication of their second-hand character.<sup>2</sup> To give them the appearance of new tires and not inform prospective buyers that they are otherwise is quite properly regarded by the Commission as a species of deception. But in one of these cases the concern had modified its selling policy pending the order of the Commission, in so far as to label and advertise its goods "reconstructed" tires. On the other hand, it continued in its advertising to give a "service guarantee," offering to replace any of its rebuilt tires at one-half price if they failed to give a service of 4,000 miles. Some of them did yield this mileage, it was proven, and others which failed were replaced as promised. In view of this fact it is difficult to locate the misrepresentation in the mileage guarantee. Nevertheless, the Commission concluded that "the advertisement tended to create belief among users of automobile tires that said tires sold by respondents could be expected to give a service of 4,000 miles,"

<sup>1</sup> This was the basis for a number of complaints and resultant orders comparable in all respects to the rebuilt tire cases. A manufacturer of rope was ordered to cease representing his product, made in large part of renovated fibres taken from old rope, as new and unused goods. *Federal Rope Co., Inc.*, 2 F. T. C. 327 (1920), modified order 5 F. T. C. 120 (1922). Likewise the marketing of repaired and rebuilt typewriters, check-writers, and adding machines by advertisements designed to convey the impression that they are new has been the object of adverse orders. See: *Typewriter Emporium*, 1 F. T. C. 105 (1918); *Check Writer Manufacturers, Inc.*, 4 F. T. C. 87 (1921); *Korb & Dwyer*, 4 F. T. C. 418 (1922). Cf., also, *Premium Electric Company*, 5 F. T. C. 385 (1923). Similarly the renaming of old motion pictures and their distribution and exhibition as new pictures has been condemned. See: *W. H. Production Co.*, 2 F. T. C. 11 (1919); *Royal Cinema Corp.*, 2 F. T. C. 88 (1919); *Eskey-Harris Feature Film Co.*, 5 F. T. C. 219 (1922); *American Film Corp.*, 6 F. T. C. 89 (1923); *Fox Film Corp.*, 6 F. T. C. 191 (1923). The last case cited was appealed to the courts, where the Commission's order was fully sustained, 296 Fed. 353 (1924).

<sup>2</sup> *Ironclad Tire Co.*, 1 F. T. C. 381 (1919); *Akron Tire Co.*, 2 F. T. C. 119 (1919); *Good Wear Tire & Tube Co.*, 2 F. T. C. 216 (1920); *Racine Tire Sales Co.*, 5 F. T. C. 327 (1922). In the last case, the respondent did make known that its goods were not new and unused but only inconspicuously, in small type.

and an adverse order was entered. It may be suggested that if the Commission were to attempt to impose generally the standard of commercial dealing implicit in this phase of its order, it might be over-reaching not only its authority but also its strength. If the ideal of absolute honesty in trade, or any other sphere of human relations, supposing it to be practicable, is ever realized, it is a reasonable certainty that it will not be through the force of governmental authority.

Analogous to the foregoing types of cases involving deceptive sales promotion policies are several complaints alleging misrepresentation of the quality of goods by means of false and misleading statements regarding their value. In some instances complaints have been directed against statements to the effect that the same quality of product is generally sold elsewhere at higher prices. Thus a mail-order lumber company advertised that it saved purchasers from \$200 to \$500 per building as compared with purchasers from other (regular) dealers.<sup>1</sup> The Commission found that this constituted an unfair method of competition and ordered the practice stopped.<sup>2</sup> Similarly a paint manufacturer was ordered to cease advertising paint which he sold at \$1.50 per gallon as being of the same grade as "paint sold under the name of 'house paint' around the city at \$2.50 and \$3.00."<sup>3</sup> In numerous other instances complaints have been directed against the marking of nominal or fictitious prices upon wrappers, packages, or containers of goods intended for sale at much lower prices.<sup>4</sup> In the razor trade this practice seems to have been very common.<sup>5</sup> Finally, there are several cases

<sup>1</sup> *Gordon-VanTine Co.*, 1 F. T. C. 316 (1919). Cf., also, *Chicago Mills Works Supply Co.*, 1 F. T. C. 448 (1919).

<sup>2</sup> It should be noted that in this case there were several other factors, supporting the charge of a general policy of competitor disparagement.

<sup>3</sup> *Wm. E. Hinch*, 5 F. T. C. 112, 119 (1922). See, also, *E. J. Brach & Son*, 1 F. T. C. 186 (1918), where the respondent firm had advertised that it was selling below cost; and *Great Eastern Wholesale Furniture Co.*, Complaint No. 1151, Annual Report, 1924, p. 229, where respondent advertised that it sold furniture at wholesale prices.

<sup>4</sup> *Holland Piano Mfg. Co.*, 3 F. T. C. 31 (1920); *Clayton E. Summey*, Complaint No. 1174, Annual Report, 1924, p. 233. See, also, account of trade practice submittal of sheet music industry, Annual Report, 1924, pp. 66-68.

<sup>5</sup> *Sheffield Razor Company*, 4 F. T. C. 373 (1922); *Solus Mfg. Co.*, 4 F. T. C. 317 (1922); *N. Shure Co.*, 4 F. T. C. 334 (1922); *Burham Safety Razor Co.*, 4 F. T. C. 363 (1922); *Geneva Cutlery Corp.*, 4 F. T. C. 368 (1922); *Henkel-Claus Co.*, 5 F. T. C. 33 (1922); *C. D. Higgins Mfg. Co.*, 5 F. T. C. 100 (1922); *Morrison & Co.*, 5 F. T. C. 189 (1922); *Eagle Safety Razor Co.*, 5 F. T. C. 172 (1922).

in which combination offers of an assortment of merchandise have been attacked on the ground that the nominal prices of the several items included in the combination were juggled so as to make it appear the value of the whole assortment was much more than its actual value and than the price charged. The sales policies of several mail-order grocery firms have been found to embody this deceptive device, and orders to cease and desist issued.<sup>1</sup> It may be observed that these cases merely present the "leader" policy, already discussed, under another aspect.<sup>2</sup> It is difficult to understand upon what ground it becomes unlawful to advertise and offer in combination a group of articles at specified prices for the several items, even though these specified prices may some be disproportionately high and some correspondingly low, if the seller has the unqualified right to offer and to sell (as he might but does not) each article singly at the announced prices. It may be ventured that when, in due course, the courts are presented with this issue they will find no more reason for holding invalid the "leader" policy under these circumstances than when it is pursued unconditionally.<sup>3</sup>

It is significant that in the two cases of this class (misrepresentation of quality or value by fictitious pricing) to be adjudicated in the courts, the Commission's orders have been reversed.<sup>4</sup> In one instance the respondent was engaged in

<sup>1</sup> *Cole-Conrad Co.*, 2 F. T. C. 188 (1919); *Commonwealth Co.*, 3 F. T. C. 46 (1920); *Liberty Wholesale Grocers*, 3 F. T. C. 103 (1920); *Big Four Grocery Co.*, 3 F. T. C. 338 (1921); *Aiben Harley*, 4 F. T. C. 31 (1921).

Paragraph 3 of the Order in the last cited case may be quoted as typical "Publishing or circulating . . . advertising matter or catalogues . . . wherein there is offered for sale . . . at a definite price, any combination or assortment consisting of well-known staple articles and also little-known articles in which combination or assortment the known staple articles are quoted at reduced prices with the intent, tendency, or effect to mislead and deceive the public into believing that the prices quoted for the little-known articles . . . are likewise reduced, when as a matter of fact such last named prices are higher than would ordinarily be charged by retailers for the said little-known articles and high enough to more than offset the alleged reduced prices . . . for . . . staple articles."

<sup>2</sup> See Chapter IV, *supra*.

<sup>3</sup> As in the ordinary case where a specially attractive bargain is offered to draw trade.

<sup>4</sup> *Chicago Portrait Co.*, 5 F. T. C. 396 (1923); 4 Fed. (2d), 759 (1924). This decision has been appealed to the Supreme Court. Petition filed, May 27, 1925. Similarly, in *John C. Winston Co.*, Complaint No. 1060, order issued August 13, 1924, the respondent was charged with having misrepresented the value of its "Winston's Loose Leaf Cumulative Encyclopedia," which it offered in conjunction with its "Annual Research Service" for \$49, after having advertised the price of same to be

selling "portraits," being enlargements from photographs furnished by customers, which were colored by hand. The complaint charged that the respondent's salesmen stated to prospective customers that they could purchase for ten dollars a picture customarily sold for twenty dollars. So-called "trade checks" were issued as an alleged special favor being offered for a limited period. The Commission had found, and the court did not question, that false representations had been made regarding the usual prices for such work as respondent did.<sup>1</sup> But that this constituted an unfair method of competition the court denied. "The company was selling family portraits," the court pointed out, "not to be worth so much money, but to be of the kind and quality of the sample there exhibited. There is no evidence or finding that any purchaser was dissatisfied because the portrait delivered was not equal to the sample exhibited."<sup>2</sup> If this is suggestive of the settled common law doctrine respecting sales by sample, it nevertheless introduces a salutary check upon the extension of commission regulation.

It may be that the ordinary buyer, the typical member of "the consuming public," is more readily deceived by a price tag or a statement of value in money terms than by "puffing" claims of quality or recommendations of an article. This appears to be the only basis upon which the finding of unfair competition in most of these cases could have been justified. That in fact fictitious price "reductions" are more deceptive than fictitious assertions of the superiority of an article may well be questioned. To mark "Price \$5.00" on a fifty-cent razor, actually offered for fifty cents, is essentially the same as stating, "This razor is worth ten times the price." Both are exaggerations and either may mislead or deceive a certain small section of the public. On this ground they are no

\$104. This case was also appealed to the courts, where the Commission's order was vacated; 3 Fed. 961 (1925). An appeal from this decision is now pending in the Supreme Court. Petition filed May 26, 1925. Cf., also, *Standard Education Society*, 7 F. T. C. 20 (1923), condemning like misrepresentation as well as other practices.

<sup>1</sup> The order of the Commission (5 F. T. C. 396, 408) required the company to cease "from representing to . . . prospective customers that the usual prices which it receives, or has received for its portraits, are greater than the prices at which similar portraits are offered to such . . . prospective customers, when such is not the fact."

<sup>2</sup> *Op. cit.*, p. 763.

doubt to be regarded as equally improper from the ethical point of view. But, as already observed, there are reasons for disputing that the sphere of coercive regulation of business behavior is or should be coeval with the sphere of ethically objectionable business conduct. Probably no one would contend that such deception as results from exuberant and excessive praise of the quality of a commodity furnishes sufficient warrant for its condemnation as unfair competition. To do so would, as has been pointed out, mean the assumption of a plainly unmanageable administrative burden. Likewise it is probable that misleading statements of value result in a negligible amount of deception in practice; and the attempt to suppress them seems likely to encounter comparable obstacles. Purely as a problem of administration, value is not easy to determine. At what point, moreover, does exaggeration become deception? And does not exaggeration carried to excess cease to deceive? Considerations such as these suggest that the Federal Trade Commission is undertaking a hazardous, if not a hopeless, task in extending its regulatory powers in this direction.

#### §4. FALSE CLAIM TO ENDORSEMENT OR USE

Closely akin to misrepresentation of quality stands sales promotion by unfounded and unauthorized claims to endorsement of government departments or public bodies. In either case the practice involves deception of buyers concerning the merits of a product, with consequent injury to competing producers,<sup>1</sup> who by implication are unable to obtain the endorsement falsely claimed. At common law, it will be recalled, this method of competition was not regarded as illegal,<sup>2</sup> but its patent unfairness has brought it well within the scope of the Federal Trade Commission's jurisdiction, with judicial sanction.<sup>3</sup> The practice seems to have received

<sup>1</sup> It should also be pointed out that a false claim to endorsement by a governmental agency may seriously affect the reputation of that agency should the product be markedly inferior. Practically, though not legally, this serves as an added ground for action by the Federal Trade Commission.

<sup>2</sup> In *Singer Mfg. Co. v. Domestic Sewing Machine Co.*, 49 Ga. 70 (1872), the plaintiff had been awarded a diploma for the best sewing machine exhibited at a state fair. The defendant had published false statements that its machine had won this distinction. The court refused the injunction sought.

<sup>3</sup> *Guarantee Veterinary Co. v. Federal Trade Commission*, 285 Fed. 853 (1922).

special impetus from the fact that the Government during the war became a purchaser of a great variety of commodities in enormous quantities. Altogether some thirty complaints have been issued charging unfair competition by this species of misrepresentation.<sup>1</sup>

The extent of the injury and correspondingly the justification of interference by the Federal Trade Commission depend largely upon the nature of the statements made and upon the degree to which they influence purchasers, which, in turn, depends in a measure upon the character of the product in question. An examination of a few of the typical cases passed upon by the Commission will serve to illustrate the bearing of these several factors as well as to indicate the policy being pursued.

Direct claims of official endorsement where this has not been granted afford the clearest examples of the unfairness of this practice. Thus, a manufacturer of spark plugs was very properly ordered to cease advertising that his product has been "certified by the Bureau of Standards of the United States Department of Commerce," when it was found that the Bureau had done nothing more than test the given spark plug at the respondent's request.<sup>2</sup> Again, a concern selling salt blocks was required to discontinue false statements in its advertising to the effect that the Government had adopted its product and purchased the company's "entire southern output."<sup>3</sup> Similarly a publishing concern selling outfits for courses in commercial subjects was restrained from advertising that the Supreme Court had decided that its book-keeping course was the best, or that the Civil Service Commission had either drafted or endorsed its instruction sets.<sup>4</sup> And another publisher, found to have falsely claimed that its reference book had been "officially adopted by 24 states,"

<sup>1</sup> Up to the end of the last fiscal year, June 30, 1924.

<sup>2</sup> *The Silvox Co.*, 1 F. T. C. 301 (1918). In a subsequent action against the same respondent and a distributing agency for making false statements that the Silvox spark plug was the result of government experimentation to develop a suitable spark plug for the Liberty Motor, another order to cease and desist was issued. It may be noted that this order was issued notwithstanding the finding of the Commission that the charges of the complaint that these false statements had the effect of deceiving the trade were not supported by the evidence. *The Silvox Co.*, 4 F. T. C. 41 (1921). See particularly page 50.

<sup>3</sup> *Guarantee Veterinary Co.*, 4 F. T. C. 149 (1921).

<sup>4</sup> *Droughton Text Book Co.*, 2 F. T. C. 388 (1920).

was ordered to cease and desist from this misrepresentation.<sup>1</sup> It appears that direct claims of governmental endorsement, when false, are unlawful without regard to the character of the commodity or the specific allegation of the mode or agency of endorsement.<sup>2</sup> In the single case of this type to be appealed to the courts, the circuit court of appeals upheld fully the findings and order of the Commission.<sup>3</sup>

Whether or not false claims to endorsement by voluntary associations having the character of semi-public bodies are to be placed upon an identical footing with the foregoing class of cases, it is certain that when deception actually results and the public is being defrauded there is abundant ground for action by the Federal Trade Commission. Thus, the Commission has exerted its authority to compel the abandonment by a soap manufacturer of the publication of false assertions that its alleged "medicated" soaps were "manufactured for," or "according to the formulæ of," the "National Medical Association" and alleged associations of physicians under other fictitious names.<sup>4</sup> These references to medical associations were clearly designed to deceive purchasers into the belief that the American Medical Association had in some way approved the respondent's products, and the Commission found they actually had that tendency. In another proceeding, the investigation disclosed that the respondent labeled its golf balls "Official" and in a printed legend on the wrappers or containers stated that the product was standard and official as required by the United States Golf Association.<sup>5</sup>

<sup>1</sup> *Standard Education Society*, Complaint No. 994. Order issued November 15, 1923, Annual Report, 1924, p. 177.

<sup>2</sup> Other cases in which the Commission has taken adverse action upon selling practices of this variety are: *Consolidated Oil Co.*, 1 F. T. C. 285 (1919); *Plunkett Chemical Co.*, 3 F. T. C. 53 (1920); *Accounting Machine Co.*, 3 F. T. C. 361 (1921); *Chemical Fuel Co. of Amer.*, 4 F. T. C. 387 (1922).

<sup>3</sup> *Federal Trade Commission v. Guarantee Veterinary Co.*, 285 Fed. 853 (1922).

<sup>4</sup> *Williams Soap Co.*, 6 F. T. C. 107 (1923).

<sup>5</sup> *Allied Golf Co.*, Complaint No. 1078, 7 F. T. C. 250 (1924). The breadth of the order in this case deserves some comment. The respondent was forbidden as label its product official, "unless and until such golf balls have been adopted as 'official' by some competent authority." This presents issues broader than those presented by the facts in the particular case. In the first place, it suggests that the Commission may ultimately have to determine what constitutes a "competent authority" to establish an official standard for golf balls, and by implication for other articles of a similar nature. Is there any occasion for its assuming this responsibility? In the second place, the order of the Commission in this case made no provision for the contingency in which a recognized professional body simply makes



The Commission found that this practice created and was intended to create the erroneous belief that the respondent's golf balls had been officially adopted by the United States Golf Association and concluded that it was unfair to competing manufacturers.

There are a number of cases in which no direct claim to use or endorsement was the basis of complaint, but only an indirect intimation to that effect. Under these circumstances the tendency to deceive may or may not exist, depending principally upon the nature of the goods. Such designations of products as "Government supplies,"<sup>1</sup> "Army and Navy Paint,"<sup>2</sup> and "Navy Architectural Spar and Interior Varnish"<sup>3</sup> are obviously suggestive of use by the national Government. They have as much of a tendency to deceive probably as an unequivocal declaration that the goods are purchased by the United States Government. On the other hand, to name a given brand of tobacco "Army and Navy Plug Tobacco," it may be supposed, would have substantially no tendency to deceive, since it is generally known that the Government does not purchase such supplies. Presumably it would not be held an unfair method of competition, therefore. It need hardly be added that the use of "United States," or "American," or the name of a state as part of a corporate name is too common to suggest to anyone that the concern has any connection with any branch of the government; and it is not unlawful.<sup>4</sup>

## §5. MISREPRESENTATION OF TRADE STATUS

Among the methods of sales promotion which involve deceit in some form and have therefore been attacked as unfair specifications regarding the size, weight, and composition of goods meeting its standard. When the product of no single manufacturer is adopted as the sole official article of the given class, would it constitute unfair competition for a manufacturer to label his goods "official" if in fact they complied with the specifications?

<sup>1</sup> *Lewis Pelstring*, 3 F. T. C. 42 (1920). Cf. *U. S. Refining Co.*, 6 F. T. C. 24 (1923).

<sup>2</sup> *U. S. Salvage Co.*, 3 F. T. C. 130 (1920).

<sup>3</sup> *C. H. Parker Co.*, 5 F. T. C. 253 (1922).

<sup>4</sup> In *Federal Bond & Mortgage Co.*, Complaint No. 1050, order issued September 2, 1924, however, the Commission required the respondent to cease describing the securities sold by it as "Federal bonds" when the bonds so described were not obligations of the United States Government. Respondent was also required to abandon its slogan: "Federal bonds are better bonds."

competition is misrepresentation of trade status. The changes which have come over the commercial structure in recent years, referred to in a previous chapter as a "commercial revolution," have attracted popular attention and given rise to more or less exaggerated notions of the possibilities of saving from dispensing with middlemen. Enterprising traders have recognized an opportunity for profit in exploiting these prevalent illusions. By holding themselves out as manufacturers "selling direct," or by other false pretensions they have sought to attract custom from sections of the buying public which they could not reach upon the basis solely of the merit of their goods in relation to their scale of prices. Sometimes this is done by direct, positive statements in advertising material.<sup>1</sup> In other cases resort is had to indirect and more subtle methods of suggesting the same misinformation, as by styling a wholesale concern a "Manufacturing Company," or a "Mill," or by inserting illustrations of factories in catalogues and on letter-heads. All of these forms of misrepresentation have been condemned by the Federal Trade Commission.

A typical example of direct misrepresentation of trade status is afforded by the proceedings against the North American Fibre Products Company.<sup>2</sup> This concern was engaged in selling varnishes, paints, and allied products which it purchased from various manufacturers, who labeled such products in accordance with its instructions. These labels bore inscriptions such as, "Manufactured Exclusively by North American Fibre Products Company," and "Sole Manufacturers, North American Fibre Products Company." The respondent made similar statements in advertising circulars, pamphlets, and letters; and it also claimed that it had factories in numerous cities throughout the country, the factory-locations listed being the places in which a manufacturer from whom it purchased part of its goods had plants. The Commission found as a fact that "the purchasing public

<sup>1</sup> There are six cases purely of this class: *Chase Shoe Co.*, 1 F. T. C. 495 (1919); *North American Fibre Products Co.*, 5 F. T. C. 410 (1923); *Lewis Feather Bed & Pillow Co.*, Complaint No. 1104, Order issued February, 1925; *American Feather Bed & Pillow Co.*, Complaint No. 1129, Order issued December 6, 1924; *Samuel Seligsohn*, Complaint No. 1135, Order issued August 5, 1924; *N. F. Fliegelman*, Complaint No. 1139, Order issued August 6, 1924.

<sup>2</sup> *North American Fibre Products Co.*, 5 F. T. C. 410 (1923).

believes that when it buys goods direct from the manufacturer it thereby saves all intermediate profits." It concluded that the practices of the respondent tended to deceive the purchasing public and to injure competitors of the respondent, and therefore constituted an unfair method of competition. An order to cease and desist was, accordingly, issued.

That the practices described above have been a common incident in many lines of business for a long period is not, of course, conclusive of their fairness or legitimacy.<sup>1</sup> It may well raise a question, however, of the justification for their condemnation. That there is deception in one sense cannot be denied. Many purchasers of the North American Fibre Products Company's brands of varnish no doubt believed they were purchasing goods made by that company. But is deception of this kind, in the absence of any evidence that the goods themselves were not of the composition and quality they were represented to be, or that the price charged was extortionate, to be raised to the rank of a violation of law? It should be noted that the Commission did not find that the practices of the respondent occasioned any injury to buyers. Indeed, it might appear that the deception amounted to no more than a means of allaying a popular prejudice.

When a trader stands responsible for the goods made by another to his order and sells them under no misrepresentation as to their quality, condition, or even value, it would seem to be an unwarrantable interference in private transactions for the government to step in merely to enforce the abstract principle of honesty. Unless the Federal Trade Commission is prepared to go the full distance of becoming an arbiter of trade morals and unless there is legislative and judicial sanction and popular support for such a course, there is no ground for accepting this particular extension of administrative authority. Suppose A, the proprietor of a department store, were to advertise in this manner: "Come to our new \$3,000,000 store to do your shopping" and listed articles which might be purchased there at specified prices. If as a matter of fact the cost of the store, including equipment, was only \$1,600,000, would this constitute an unfair

<sup>1</sup> See opinion of Supreme Court in *Federal Trade Commission v. Winsted Hosiery Co.*, 258 U. S., 483, 484 (1922).

method of competition? Is there any less likelihood that the purchasing public would be "deceived" by (i. e., would accept as true) this statement than by the statements upon which the charge against the North American Fibre Products Company was based? In both cases there is misrepresentation. In neither case has the misrepresentation any connection whatever with the terms of the bargain to be negotiated. It therefore has no essential relation to the fairness or unfairness of the business transactions of the party making the misrepresentation, though it may not exhibit that scrupulous adherence to the truth which is admittedly the ethical ideal. It is submitted that for misrepresentation to amount to a legal offense it must be proven that it has a substantial tendency not only to induce actions which might not otherwise be taken, but to do so *to the injury* of the parties deceived.<sup>1</sup> In any other circumstances the indirect or consequential damages which might, still, be suffered by third parties, such as the competitors of the seller, must be held to be irremediable, *damnum absque injuria* in the terms of the lawyer, if any freedom is to be left in trade competition.

Indirect devices for suggesting that a seller has a particular trade status which he does not actually occupy might seem to be even more innocuous than direct misrepresentations of this character. Nevertheless the Commission has found occasion for issuing orders against this method of misrepresenting trade status more frequently than against the direct method,<sup>2</sup> and it has been supported in its policy by a recent judicial decision upholding one of these orders.<sup>3</sup> These

<sup>1</sup> As was stated by the court in the recent case of *Chicago Portrait Co. v. Federal Trade Commission*, 4 Fed. (2d), 763 (1924), vacating the Commission's order: "The purchaser might have been deceived in some small way, but certain it is that he was not injured, nor was any competitor injured."

<sup>2</sup> The list of orders includes six cases based merely on suggestions and five others in which the use of a misleading firm name was coupled with false statements in advertising. In the first group are: *Household Storage Co.*, 3 F. T. C. 163 (1920); *Solus Mfg. Co.*, 4 F. T. C. 317 (1922); *Pure Silk Hosiery Mills*, 5 F. T. C. 245 (1922); *Wasatch Woolen Mills*, 7 F. T. C. 62 (1923); *Jenkins Knitting Mills Co.*, 7 F. T. C. 68 (1923); *Salt Lake Cooperative Woolen Mills*, 7 F. T. C. 370 (1924). In the second group are: *United Woolen Mills*, 6 F. T. C. 155 (1923); *Durable Pure Silk Hosiery Co.*, 7 F. T. C. 426 (1924); *Hercules Hosiery Mills*, Complaint No. 1107, Order issued October 29, 1924; *Hagen Import Co.*, Complaint No. 1217, Order issued November 7, 1924; *Superior Woolen Mills*, Complaint No. 918, Order issued December 8, 1924.

<sup>3</sup> *Federal Trade Commission v. Pure Silk Hosiery Mills*, 3 Fed. (2d) 105 (1925).

cases may be illustrated by the proceedings against the Pure Silk Hosiery Mills, which were reviewed in the courts. The respondent was a distributing concern selling silk hosiery directly to consumers, its business being done mostly if not entirely through the mails. The Commission found that the use of the word "Mills" in the respondent's trade name tended to deceive purchasers into the belief that they were buying of manufacturers, and ordered respondent to cease such use "unless and until . . . (it) . . . actually owns or operates a factory . . . in which hosiery sold by . . . (it) . . . is manufactured." Subsequently the respondent purchased a minority interest in a hosiery mill and refused to change its corporate name. Thereupon the Commission made application for an order of enforcement, which was granted, the court holding that compliance with the order necessitated an actual ownership or a direct and absolute control of a factory. The authority of the Commission in the premises seems not to have been seriously questioned by the respondent which based its case primarily on the issue of what would satisfy the order. For this reason, and pending a consideration of the subject by the Supreme Court, it seems permissible to entertain grave misgivings about the validity of the Commission's action in this and similar cases.<sup>1</sup> And it is still more open to question that the policy they embody is economically sound. Strictly applied, the principle would require a change of name every time a business concern extended its range of operations, unless it adopted at the outset an ambiguous name. And is it any less misleading for a manufacturer of shoes, styled the Standard Shoe Company, to engage in the business of buying and selling dressed leather, than it is for a shoe dealer, who does not manufacture shoes, to adopt the corporate name of the Standard Shoe Manufacturing Company? There is misrepresentation in either case. But as has previously been sug-

<sup>1</sup> The Commission appears clearly to have gone to extremes in issuing a complaint against the Consolidated Woolen Mills because, as it was averred, the respondent was "not a consolidation of woolen mills, but is a consolidation of two knitting mills." The complaint was only dismissed when the respondent had changed its name to the "Consolidated Knitting Mills Company." Complaint No. 1003, Dismissed November 8, 1923. It should be added that there was no question in the case regarding the material which respondent worked up into finished goods. It was wool.

gested, there are certainly some forms or degrees of misrepresentation which, if they mislead at all, do not do so in a manner and to an extent to give ground for setting in motion the costly machinery of government prosecution.

#### §6. MISREPRESENTATION OF ORIGIN

Industrial specialization manifests itself in one way by a tendency of certain types of industry towards geographical concentration. This is frequently referred to as localization of industry and is exemplified by the collar industry, which is centered in Troy, New York, and the furniture industry, which is centered in Grand Rapids, Michigan. In some instances, though not so frequently as in the handicraft era, a reputation for quality comes to be attached to the products, from whatever establishment, of these specialized industrial centers. This factor of "place good-will" attaches much more commonly nowadays, however, to the products of a region than of a single locality. This is for the reason that climatic and physiographic factors still exercise a dominant influence on productive processes in some branches of industry, notwithstanding the progress of mechanical and chemical technique. In either case, there is a temptation to manufacturers located elsewhere to take advantage of the "place good-will" of the well-known city or the favored region by misrepresenting the origin of their product.

Whether or not this misrepresentation constitutes an unfair method of competition would seem to depend entirely upon the special circumstances of each case. The most significant circumstance is undoubtedly the extent to which the purchasing public identify a place with a certain standard of quality in a given product. Thus, to take two extreme examples, Cordovan leather has long since ceased to mean to the trade or to the public generally leather tanned in Cordova, Spain, while a Panama hat does signify a hat made of straw grown and woven in tropical America.<sup>1</sup> To attempt to en-

<sup>1</sup> A series of recent cases well illustrates the enigma which must frequently confront the Commission in determining when misrepresentation of origin amounts to an unfair method of competition. Six complaints (Nos. 1270-1275 incl.) have been issued (February 13, 1925) against importers of lace from China who advertise their goods as Irish lace. Does Irish lace signify a certain type of pattern, design, or stitch, or does it signify lace made in Ireland?

force upon the tanning industry the rule that no leathers should be described as "Cordovan" which were not in fact of Spanish origin would be patently absurd. Yet it would appear that the Federal Trade Commission has endeavored to "reform" the silver plating industry in a comparable manner.

In a trade practice submittal before the Commission in 1922 practically one-half of the silver plate manufacturers assembled to consider the use of the term "Sheffield" as applied to silver plated ware.<sup>1</sup> The term originally designated, it appeared, a method which was developed in Sheffield, England, of manufacturing silver ware by applying sheets of silver to a base of other metal and rolling the combination into the desired shape. Subsequently this process was superseded by the modern method of electrolytic plating and true Sheffield ware disappeared from the market, except in antique shops. The term "Sheffield," however, survived in the industry, though in losing its old meaning it acquired no definite and accepted connotation in the trade. It came to be applied indiscriminately to all grades of silver plated ware. Despite the indefiniteness in the trade use of the term the Commission insisted that "to the purchasing public the term is an indication of origin in Sheffield, England, and signifies quality, not perhaps accurately measured but a quality of appearance and durability of service corresponding in some degree to the quality which characterized the original ware." If this meant anything at all and indicated the policy proposed to be followed by the Commission, it meant an assumption of an authority quite beyond the jurisdiction of even a federal commission. The quality of plate produced and sold by a manufacturer located in Sheffield, England, is not a matter within the purview of the regulatory power of any agency of the United States Government. That such ware, no matter how inferior in quality, is subject to importation, bearing the "Sheffield" mark, is at least by implication granted by the Commission and, unless there were direct misrepresentation, could not be denied. It follows that the Commission's proposed policy, calling for the feat of riding two horses at once, was impracticable and

<sup>1</sup> Federal Trade Commission, "Trade Practice Submittals, 1919-1923," p. 43.

unenforceable. If, on the other hand, the Commission was really proposing only to defend the "geographical integrity" of the Sheffield stamp, notwithstanding the broad statement quoted, then its policy, while understandable, appears to be of questionable expediency.

At the conference, while a few of the manufacturers favored acceptance of the Commission's policy and abandonment of the term "Sheffield" altogether, it was finally agreed to meet the Commission halfway. A trade definition was adopted to the effect "that the word Sheffield as a mark for silver plated hollow ware means quality; that, furthermore, quality is defined as meaning an article well plated on a base metal of nickel silver of not less than ten per cent nickel plate, and that the same may have Britannia metal trimmings and mountings." Exhibiting an inflexible adherence to its original proposal the Commission has brought a number of complaints, since the conference on the trade practice submittal, against American manufacturers stamping their silver plate ware "Sheffield."<sup>1</sup> One of these complaints even charges that it is unfair competition to mark plate of American origin "Sheffield plate made in U. S. A."<sup>2</sup>

That genuine deception may be perpetrated by ascribing a false origin to certain merchandise, however, is plainly illustrated in some of the other complaints of this description. The use of the word "Tampa" in connection with the sale of cigars not made in the Tampa district has been condemned,<sup>3</sup> and as the tobacco grown in the territory around that city has a special quality, such an order tends to prevent deception of buyers that actually works to their damage. Even clearer is the case for suppressing the misrepresentation of cigars by the use of words indicating a Cuban origin. These cases

<sup>1</sup> There are fifteen cases of this nature. The docket numbers of the complaints are: 1066, 1067, 1068, 1094, 1097, 1131, 1155, 1156, 1158, 1159, 1160, 1161, 1162, 1163, 1200, 1234. On May 16, 1925, it was announced that orders to cease and desist had been issued against the respondents in four of these complaints, numbers 1094, 1155, 1161, and 1200.

<sup>2</sup> *Abraham Ash Co.*, Complaint No. 1161, Annual Report 1924, p. 231. In the order this qualification is disregarded.

<sup>3</sup> *G. F. Hemler*, 6 F. T. C. 159 (1923); *Kraus & Co.*, 6 F. T. C. 207 (1923); *King-Ferree Co.*, 6 F. T. C. 253 (1923); *C. N. Dellenger & Co.*, Annual Report 1924, p. 188. Another complaint of this character was recently dismissed because respondent had established a factory in Tampa. *H. M. Triggs Cigar Co.*, Complaint 1207. Dismissed April 24, 1925.



border closely on misbranding, it may be observed, since "Havana," as the term has come to be used in the trade, refers to a type or quality of tobacco leaf almost as much as to place of origin.<sup>1</sup> In the cases attacking the practice of selling safety matches made in Japan in boxes bearing labels with distinctive Swedish words and imitative pictures of medals awarded Swedish manufacturers at various European expositions, the deceit is manifest.<sup>2</sup> In the absence of evidence that the Japanese product was in any way inferior to the Swedish safety match, however, it may be ventured that the basic ground for the orders to cease and desist in these cases is to be found in the analogy to trade-mark simulation. In such cases, where the pirating is of private and not national marks, it is the injury to the producer whose goods are imitated, rather than the deception of the ultimate buyer, which affords the primary ground for relief. The same consideration would seem applicable here.

Finally, it may be pointed out that the protection of neither the buying public nor the competing producers requires literal accuracy in representing the origin of goods. For example, to describe an automobile manufactured in Hamtramck, Michigan, a suburb of Detroit, as a product "Made in Detroit" could give no just occasion for reproach, let alone for prosecution. Nevertheless, in a proceeding against the Geneva Watch Company, a concern engaged in importing watch movements from various points in Switzerland, the Federal Trade Commission ordered the use of the respondent's name and of the word "Geneva" to be discontinued unless there should be in equally conspicuous type the names of the several towns in which respondent's goods were manufactured in Switzerland.<sup>3</sup> While Swiss watches undoubtedly enjoy a peculiar reputation in the market,

<sup>1</sup> *James B. Hall, Jr., Inc.*, Complaint No. 1137, Order issued July 29, 1924; *Edwin Cigar Co.*, Complaint No. 1138, Order issued July 29, 1924; *G. F. Hemler*, 6 F. T. C. 159 (1923). There are other cases in which the use of misleading terms such as "Habanoes" has been condemned.

<sup>2</sup> *Cupples Co.*, 3 F. T. C. 407 (1921); *Taiyo Trading Co.*, 3 F. T. C. 199 (1921). Similar issues were presented by two complaints against representation of American made cotton fabrics as "English broadcloth." *Katz & Davidson*, Complaint No. 1065, Annual Report 1924, p. 217. Order issued July, 1924. *F. Jacobson & Sons* Complaint No. 1173, Order issued August 7, 1924.

<sup>3</sup> *Geneva Watch Co.*, 6 F. T. C. 452 (1923).

which is deserving of protection, there seems little reason for believing that the general public would make any distinction between Swiss watches made in Geneva and Swiss watches made elsewhere in Switzerland, were they apprized of the precise facts. This serves to emphasize the necessity, remarked at the outset, of close scrutiny of the surrounding circumstances in cases of this class to determine that misrepresentation does actually tend to deceive. Unless administrative regulation takes into account the peculiarities of each case and applies this general principle with a nice discrimination, it is in danger of subjecting those having the responsibility to the charge of bigotry.<sup>1</sup>

#### §7. FALSE PACKAGING

An insidious form of commercial misrepresentation, which is occasionally uncovered, relates to the quantity of goods in a given container. Packaging of merchandise by producers has become much more prevalent in recent years as a means of product identification in connection with the development of national advertising by manufacturers. As a matter of convenience, no less than of tradition, these packages tend to become standardized in many lines of trade at sizes which will accommodate measured portions of the product corresponding to well-recognized units of weight, volume, or length. The misrepresentation of quantity, to which this practice readily lends itself, is achieved by the retention of the customary size of package while reducing the usual amount of goods contained in such packages. This is the sole method of quantity misrepresentation against which the Federal Trade Commission has had occasion to issue complaints. Direct falsehoods concerning the amount of goods sold seem to be no longer tolerated in trade circles, and if they occur now and then the rights of the injured parties to redress are so clear and certain that the intervention of a public agency is not required.

The cases upon false packaging thus far determined by the

<sup>1</sup> It is not difficult to imagine the absurdities which might result from a campaign of absolute repression of misrepresentation, regardless of actual deception. There might eventuate a dearth of "Eskimo pies" and, under present conditions, of Russian caviar.

Commission relate with one exception to the marketing of butter.<sup>1</sup> In the creamery cases, which were similar in essential respects, the respondents were found to have put up their products in the regular cartons for one pound, eight ounces, and four ounces of butter, though the amounts these cartons actually contained were from a fraction of an ounce to two ounces less than the mentioned quantities. The Commission concluded quite justly that this placed an instrument of fraud in the hands of dealers, and that the practice created a strong tendency towards the deception of consumers to their damage. In each of these cases, it appeared, the outer wrapper or carton bore a statement of the actual net weight of butter contained in the package. Not only the fact that this declaration of weight was not conspicuous, but the fact, as established by the Commission, that many if not most retail customers received the butter only in the inner wrapper and did not ordinarily see the outer carton at all, prevented this notice from offsetting the tendency to deceive.

It may be observed that the extent to which deceit is actually accomplished by such methods of packaging depends upon the extent to which custom has crystallized around certain standards of measurement in handling particular commodities. In the sale of butter there is no question but that the 16-ounce pound is the accepted unit of measurement in distribution. For the dairyman to simulate the packages ordinarily used as containers for that amount is to become an accessory in the perpetration of a palpable fraud. But there are other commodities, such as drugs and liquid toilet preparations, which are not customarily sold in any standard quantities, and it probably would not constitute an unfair method of competition, therefore, to put up such preparations in bottles of any size or shape. It is well recognized that bottles used as containers for such preparations are not only not standardized but are designedly misleading in many instances. By that very fact, however, they cease to be

<sup>1</sup> *Mountain Grove Creamery*, 6 F. T. C. 426 (1923); *Wichita Creamery Co.*, 6 F. T. C. 435 (1923); *Meriden Creamery Co.*, 6 F. T. C. 444 (1923); *Ozark Creamery Co.*, Complaint No. 1221, Order issued February, 1925. See also: *Baltimore Paint & Color Works, Inc.*, Complaint No. 1265, Order announced July 15, 1925. In addition to enjoining the use of the word "Army," the Commission in this case forbade the sale of paint in containers of standard size but containing less than the standard quantity, unless this fact was clearly indicated on the container.

effective instruments of fraud, and provided no false statements are made regarding the volume of their contents it is unlikely that misleading packaging of drugs and toilet preparations would be held unlawful.

Somewhere between these extremes lies the case which has been presented by a trade practice submittal in the macaroni industry.<sup>1</sup> The Federal Trade Commission accepted the resolutions of the conference of package macaroni manufacturers condemning the sale of slack-filled packages as an unfair method of competition. "It was generally agreed," runs the official report, "that 'slack-filled' may be applied to the package with cubic contents [which,] for the bulkiest product, is so great as to enable it to contain from one and a half to two ounces more net weight than is actually placed in it."<sup>2</sup> Since there is no standard unit of measurement employed in the packaging of macaroni it is doubtful whether the Commission could enforce this resolution, however desirable such action might be. The purchasing public is not so credulous as to believe that all non-transparent containers of commodities are completely filled, and it is probable that over-size macaroni packages would be one instance in which few buyers would be deceived. At any rate, the Federal Trade Commission has taken no formal action to prevent "slack-filling" in this industry.

### §8. LOTTERIES

As a method of sales promotion, lotteries are so unusual as to warrant but passing notice. They are unusual because they were well known to be opposed to public policy even prior to the enactment of the regulatory legislation of 1914, and in some states they have been made penal offenses by statute. The reasons for this general condemnation of lotteries are primarily ethical and not economic. It is regarded as contrary to sound morality that men should be encouraged to seek "something for nothing"—or for a trifle. At the same time it is recognized that there are economic

<sup>1</sup> Federal Trade Commission, "Trade Practice Submittals, 1919-1923," p. 19.

<sup>2</sup> *Ibid.*, p. 24. The meaning of this passage, without the insertion of the bracketed "which," is obscure to say the least; and even as it is given above the effect of its faulty construction has not been entirely overcome.

objections to a scheme which extracts small contributions from many, without compensation, for the benefit of the chance recipient of an unearned prize. The suppression of lotteries, therefore, looks to the protection of the purchasing public more than to the protection of the interests of competitors. So well established is this principle that in the proceedings by the Federal Trade Commission directed against the conduct of lotteries as an unfair method of competition, the customary "finding" of a tendency to injure competitors has in most instances been omitted.

Complaints involving lottery sales methods have been issued by the Commission in some twenty-eight cases. Of these, twenty-three were filed at the same time, April 19, 1918, against various tea and coffee distributors.<sup>1</sup> The exact nature of the lottery method used is not described in these complaints nor in the findings of fact in the single case of the group fully reported.<sup>2</sup> In a subsequent case, against another concern in the same line of trade, the findings revealed the use of coupons redeemable in various prizes.<sup>3</sup> In each fifty-pound lot of coffee packed by the respondent in one-pound packages there were forty-five coupons entitling the holder to a bar of candy, two coupons good for one package of jell powder each, two coupons good for one can of baking powder each, and one coupon good for a sack of flour. It is probable that the other cases involved similar lottery methods. The orders issued in all of these tea and coffee cases directed the respondents, in similar language, to cease and desist offering coupons redeemable in prizes "the distribution of which . . . is determined by chance or lot."

The policy adopted by the Commission in these cases comports with established public policy. There was no finding that the prizes were misrepresented, that their drawing was dishonestly conducted, or that the quality of the coffee sold by the lottery method was inferior. Indeed, the Com-

<sup>1</sup> Complaints No. 98 to 120, inclusive. The eighteen cases in which orders were issued are all reported together in 1 F. T. C. 159, 163 (1918). The several dismissals are reported in 1 F. T. C. 538. The grounds for dismissal were want of jurisdiction in interstate commerce in three instances, lack of evidence in one instance, and discontinuance of practice in the other.

<sup>2</sup> *Buddha Tea Co.*, 1 F. T. C. 159 (1918).

<sup>3</sup> *Everybody's Mercantile Co.*, 3 F. T. C. 60 (1920).

mission went so far as to declare in one case that the quality of the coffee so sold was "substantial," whatever that may mean.<sup>1</sup> In other words an honest lottery as a method of promoting sales was held to constitute an unfair method of competition. This appears to be sound doctrine. If it is unfair competition to tempt buyers by misrepresentations of the quality of goods, it may be regarded as likewise unfair to tempt them to buy goods not upon their merits but upon the chance of securing something for nothing. Nevertheless, in two subsequent cases involving lottery methods of sales promotion the gist of the complaints, as of the orders, was shifted to false representations concerning the conduct of the lottery.<sup>2</sup> The respondents in both of these cases were tailors who solicited custom through an installment-lottery plan. Customers, after making a specified number of weekly payments in advance, were, according to the plan, to be divided into groups and one from each group was to be selected each week by chance to receive his clothing forthwith and without further payments. The Commission found that the representations were not fulfilled or the plan honestly carried out in either case, and on this ground issued orders to cease and desist. There seems to be no basis for such a departure from the attitude earlier taken by the Commission toward the lottery method of sales promotion. It may be noted that in a subsequent complaint against a candy manufacturer the use of lotteries in selling campaigns was again directly attacked.<sup>3</sup> This case has recently been dismissed, however, no reasons being assigned.

### §9. MISREPRESENTATION IN THE SALE OF SECURITIES

In ultimate analysis stocks and bonds are economically indistinguishable from other commodities bought and sold in the market. They are items of wealth, sources of income. To be sure, they are only tokens. As things, simply, they are worth nothing; but as evidences of interests, or as the French say "*choses en action*," they have value. In this

<sup>1</sup> *Everybody's Mercantile Co.*, 3 F. T. C. 60, 63 (1920).

<sup>2</sup> *Budd Tailoring Co.*, 5 F. T. C. 207 (1922); *Dixie Tailors*, 6 F. T. C. 486 (1923).

<sup>3</sup> *Robert F. MacKenzie Co.*, Complaint No. 1167, Annual Report 1924, p. 232. Dismissal announced, May 30, 1925. See also *Reed and Co.*, 7 F. T. C. 387 (1924).

respect they are not greatly different from some other commodities, e. g., the autographs of famous men. It is the peculiarity of all token wealth, however, that it is especially subject to fraudulent misrepresentation in market transactions. The seller cannot be immediately checked up on his statements regarding the merits of what he offers. The temptation to exaggeration and even fraud is, therefore, unusually great. Companies are formed for the primary object of selling stock for the enrichment of promoters by means of unearned commissions and salaries, and by other devices not in the interest of stockholders. Such enterprises thrive particularly in those industries in which wealth is rapidly created and, alas! frequently rapidly lost. The possibilities of sudden affluence by the opening of a single oil well have been capitalized innumerable times with disastrous results to unwary investors. New inventions, like the radio, also are the basis for many fraudulent promotions. For these reasons it has been found necessary in a majority of states to provide statutes regulating in detail the issuance of securities. These are generally known as "blue-sky" laws, and proposals for legislation of the same character have long been pending in Congress. Up to the present time there has been no federal action taken specifically to control the interstate distribution of securities. The general statute against using the mails to defraud has, however, been invoked in cases in which the character of the selling methods employed made it applicable.

The extent of the frauds being perpetrated by misrepresentation of securities sold in interstate trade and the inadequacy of the remedies against these transactions brought the subject to the attention of the Federal Trade Commission. That the Commission had jurisdiction on the ground that interstate commerce was involved was readily determined and the Commission also decided that fraudulent misrepresentation of securities constituted an unfair method of competition. The Commission took the view that a corporation and its promoters engaged in selling worthless securities by means of false advertising were in competition with the many firms engaged in selling the stocks and bonds of legitimately organized companies. That the widespread marketing of shares in oil companies having no genuine pros-

pects of petroleum production, for example, tends to discredit securities representing real investment values, not only in the oil industry but in other industries as well, can scarcely be doubted. Investment banking firms pursuing legitimate business methods are unreasonably handicapped. On these grounds, the Commission assumed jurisdiction and in the five years since 1919 has issued altogether some forty-one complaints against the practice of misrepresenting securities. Of this number fifteen have resulted in orders to cease and desist, while thirteen have been dismissed and a like number are now pending. It is noteworthy that of the whole number of complaints issued all save two have related to the oil industry.<sup>1</sup>

The policy of the Federal Trade Commission appears to have been to confine the institution of proceedings against misrepresentation in the sale of securities to cases involving the elements of legal fraud. In other words, it has not sought to establish a more rigorous regulation of security issues than is provided in general by existing law within the several state jurisdictions. The Commission has been content to "fill the gap" as an agency for restraining the sort of stock frauds which state laws generally condemn but cannot reach when perpetrated in transactions flowing over state boundaries. That a somewhat more virile and scrupulous rôle might not be assumed within the ambit of Section 5 of the Federal Trade Commission Act is by no means clear.<sup>2</sup> But in view of the inadequacy of the remedy which this procedure affords for fraudulent company promotions and fraudulent sales of stocks, the course taken by the Commission was undoubtedly politic.

The shortcomings of the Commission's procedure in coping with this evil arise, first, from the fact that the Commission has no means of keeping advised of company promotions at their inception, so that by the time a case is brought to its

<sup>1</sup> These two were the *Pan Motor Co.*, 2 F. T. C. 413 (1920), and the *Ward & Mackey Biscuit Co.*, Complaint No. 347, Dismissed June 11, 1921, 3 F. T. C. 437. The abandonment of this fraudulent project was the ground for the dismissal of the case.

<sup>2</sup> The precise limits of what is legitimate in the way of promoter's fees, for example, are not settled even in ordinary practice. It is not inconceivable that a fee might be large enough to render the negotiation of sales of the company's stock "unfair competition," though not sufficiently excessive to render the flotation a fraud, justifying suits to establish the personal liability of the promoter.



attention usually the scheme is well under way and sales are in progress.<sup>1</sup> In the second place, the machinery of the Commission works slowly and during the period of investigation, answer, and the taking of testimony, the business of mulcting the public continues without interruption. Even the cease and desist order does not compel any cessation, and not until the matter is taken to a circuit court of appeals and an order of enforcement obtained, is there any stay in the nature of an injunction, disregard of which carries a penalty. From this it appears that, as the Commission has itself recommended,<sup>2</sup> the nature of the stock frauds evil is such as to require the enactment of specific regulatory legislation by Congress.<sup>3</sup>

<sup>1</sup> The costly consequences of delay are well illustrated by the facts brought out in the very first case of this character prosecuted by the Commission, *Pan Motor Co.*, 2 F. T. C. 413 (1920). One Samuel G. Pandolfo who was also a respondent in this action had organized a company for the manufacture of automobiles. The shares of stock of a par value of \$5.00 were offered for subscription at \$10.00 under an agreement that the subscriber would be entitled to purchase an automobile "for personal use" at a 15 per cent discount, in consideration of which the subscriber granted the directors the right to use the half of his subscription representing a premium "for any and all purposes for the benefit of the company within their discretion." Under this subscription agreement, the Commission found that the promoter who of course controlled the nominal board of directors, "was permitted and allowed to retain the first \$5 paid upon each share of stock." Prior to the commencement of the proceedings, stock to the par value of \$2,064,923.06 had been sold and additional subscriptions aggregating \$1,042,866.94 had been received. No less than 54,000 subscribers were of record, of whom some 39,000 had fully paid their subscriptions. Over \$1,150,000 had been expended in a sales campaign, in which the advertising had been featured by many false and misleading statements, not only with regard to the product of the company and the character of its management, but also with regard to the distribution of the stock and its value. The Commission's order, in broad terms, required the respondents to cease and desist from "publishing, advertising or circulating, false, misleading, or unfair reports or statements concerning the plan of organization, the assets, resources, business, . . . or financial standing of the Pan Motor Co., or concerning the value of the stock thereof." It is not of record what the result of this order was upon the business of the company, but that it would have served its purpose far better had it been issued in the form of an injunction at the time of the organization of the company is evident.

<sup>2</sup> Annual Report, 1919, p. 47.

<sup>3</sup> Several bills have been proposed in Congress to this end. In the 67th Congress, 2nd Session, two bills were introduced: H. R. 10102 and H. R. 10645. The former measure known as the Denison bill was favorably reported by the Committee and as H. R. 10598 in amended form was passed by the House. This bill was directed to preventing the use of the mails either for transporting securities issued contrary to the laws of the states or for promoting or procuring the sale of such securities. The other bill, H. R. 10645, would have authorized the Federal Trade Commission to require reports from persons, firms, or corporations who offer for sale in interstate commerce, stocks, bonds, and securities.

In the 68th Congress, 1st Session, a bill framed on the model of the Denison bill was reintroduced, H. R. 4, as was also another bill granting the Trade Commission authority to require reports, H. R. 80. A more comprehensive measure was introduced in the Senate in the same Session by Senator Capper, S. 1596.

## §10. COMMERCIAL BRIBERY

The offering of gifts, or in current phrase "treating," as a method of promoting sales has been a common practice from time immemorial. Indeed, students of anthropology incline to the view that all trade originated in the exchange of gifts,<sup>1</sup> discrediting Adam Smith's hypothesis of an innate "Propensity to truck, barter, and exchange one thing for another."<sup>2</sup> However this may be, the giving of presents to induce sales has long been an accepted custom in trade. Moreover, the distinction between innocent "treating" and commercial bribery is by no means clearly drawn in practice, however sharply they may be differentiated in theory. The real evil in the offering of gifts to promote sales appears to lie in the tendency to induce a breach of faith, and it is obvious that this cannot be the result if the recipient of the favors is himself the prospective customer. It is sometimes sought to distinguish treating from bribery on the basis of the amount or character of the gifts presented but while this distinction may be helpful it should be plain that it is not feasible to make the size of the gift the sole criterion of its legitimacy. The gradation from cigars to yachts and from dimes to dollars is too minute. But whenever there is inducement to an employee to act contrary to the interests of his employer, or to an agent to act contrary to the interests of his principal, the transaction savors of corruption. And the trader who seeks thus to promote his sales is engaged in an unfair method of competition, for he interposes an obstacle to the competitive opportunity of other traders, which is in no way related to any economic advantage possessed by him. The practice tends to prevent the consideration of the goods offered by the several competing manufacturers or traders strictly on the basis of their relative merit.

But, as suggested, not under all circumstances is the offer of gifts even to persons in a fiduciary relation to the real buyer unfair. For it hardly tends toward corruption to extend the ordinary courtesies and civilities of friendly companionship to business intercourse. "Treating," in an un-

<sup>1</sup> Cf. Thomas, W. I., "Source Book for Social Origins," Boston, 1909, p. 113.

<sup>2</sup> Adam Smith, "The Wealth of Nations," Book I, Chap. 11 (Cannan's edition, Vol. I, p. 15).

concealed way, to the minor extent which is so common that employers generally must be taken to be aware of its existence, could but poorly serve an ulterior motive. But when ordinary entertainment becomes so lavish as to suggest attempted corruption a different case is presented. As stated, no clear and distinct line can be drawn, but it would appear that unfair commercial bribery is present only when the practice is furtive in character and corrupting in effect.

At the very outset of its career the Federal Trade Commission undertook a vigorous campaign against commercial bribery, and during the ten years of its existence it has issued upwards of two hundred complaints against this practice. The Commission took the extreme position, in the beginning, that even the presentation of cigars or the invitation to a theatre amounted to an infraction of the law.<sup>1</sup> This was held, however, upon review of one of its orders in the circuit court of appeals, to be an unwarranted exercise of administrative authority.<sup>2</sup> The New Jersey Asbestos Company, the respondent in the case appealed, admitted that its salesmen had supplied liquors, cigars, meals and theatre tickets to the employees of its customers. The charge of giving valuable presents and sums of money, a part of the original complaint, was abandoned by the Commission. In reversing the Commission's order to cease and desist, the court declared, "The payment of money or the giving of valuable presents to an employee to induce him to influence his employer to make a contract of purchase is a fraud justifying the discharge of the employee, and perhaps the recovery by the purchaser of the amount or value of such inducement from the seller, upon the theory that it must have been included in the price. But even in such a case we think it would be a matter between individuals, and not one so affecting the public interest as to be within the jurisdiction of the Commission. . . ."<sup>3</sup>

Although this language indicates that the court regarded commercial bribery as a business method entirely outside the scope of the Commission's authority, the Commission has

<sup>1</sup> *Printers' Roller Co.*, 1 F. T. C. 240 (1918); *New Jersey Asbestos Co.*, 1 F. T. C. 472 (1919); *Roma Soap Mfg. Co.*, 1 F. T. C. 484 (1919).

<sup>2</sup> *New Jersey Asbestos Co. v. Federal Trade Commission*, 264 Fed. 509 (1922).

<sup>3</sup> *Ibid.*, p. 511.

declined to accept this construction of its powers. While choosing not to contest further the propriety of its order in this particular case, it has nevertheless continued to issue complaints and orders to cease and desist in cases where it had reason to believe that actual money bribes had been given.<sup>1</sup> In one noteworthy instance the Commission found that the respondent, a manufacturer of glue, had paid secret commissions of five per cent to a factory superintendent in the employ of a phonograph company on all respondent's sales to that company.<sup>2</sup> The bribes amounted to about \$34,000 in a period of less than two years. The validity of the Commission's order in this case has not been challenged in the courts, nor is it likely to be. That it has authority to act in such situations seems indisputable. At any rate, the Commission has proceeded to clean up certain industries in which this abuse had become prevalent. Among the more conspicuous of these were the paint and varnish industry,<sup>3</sup> the dye industry,<sup>4</sup> the road machinery industry,<sup>5</sup> and the ship chandlery trade.<sup>6</sup> In one proceeding

<sup>1</sup> Among recent complaints filed against commercial bribery are: *Johnson Process Glue Co.*, Annual Report 1924, p. 216, Order issued, April, 1925; *The Worrall Mfg. Co.*, Complaint No. 1053, Annual Report 1924, p. 216; *U. S. Oil Co.*, Complaint No. 1175, Annual Report 1924, p. 233; *Reliance Varnish Co.*, Complaint No. 1208, Order issued November 28, 1924; *Chemo Co., Inc.*, Complaint No. 1218, Order issued November 28, 1924.

<sup>2</sup> *Baeder, Adamson Co.*, 4 F. T. C. 129 (1921).

<sup>3</sup> *Reliance Varnish Works*, 1 F. T. C. 98 (1918), and forty-one cases against other paint and varnish manufacturers in which orders were issued by consent. These cases are not reported but citations are listed 1 F. T. C. 103-105 (1918). *Essex Varnish Co.*, 1 F. T. C. 138 (1918); *Twin City Varnish Co.*, 1 F. T. C. 190 (1918); *Royal Varnish Co.*, 1 F. T. C. 194 (1918); *Carter Paint Co.*, 2 F. T. C. 181 (1919); *Sealwood Co.*, 4 F. T. C. 65 (1921); *Beckwith Chandler Co.*, 4 F. T. C. 108 (1921).

<sup>4</sup> *Federal Color & Chemical Co.*, 2 F. T. C. 71 (1919); *F. E. Atteaux & Co.*, 2 F. T. C. 82 (1919); *U. S. Color & Chemical Co.*, 3 F. T. C. 313 (1921); *Ricco Co., Inc.*, 3 F. T. C. 418 (1921); *United Indigo Chemical Co.*, 3 F. T. C. 425 (1921); *United Chemical Products Co.*, 4 F. T. C. 220 (1922); *Dudley D. Gessler*, 6 F. T. C. 180 (1923).

<sup>5</sup> *Russell Grader Mfg. Co.*, 5 F. T. C. 77 (1922); *Austin Western Road Machinery Co.*, 5 F. T. C. 82 (1922). Similar orders were issued in three other cases cited on p. 86. *Stockland Road Machinery Co.*, 5 F. T. C. 87 (1922).

Subsequently a second hearing was held and a modified order issued in the proceeding against the Austin Western Road Machinery Company, in which the Commission took account of an attempted evasion of its first order and added to the previous restrictions by forbidding the respondent to employ public officials as agents or to give valuable gifts to their relatives. 6 F. T. C. 69 (1923).

<sup>6</sup> *Sparrows Point Store Co.*, 3 F. T. C. 20 (1920); *Flood & Calvert*, 3 F. T. C. 205 (1921), and twenty-four cases decided at the same time, and cited on p. 208 as similar; *John R. Adams & Co.*, 3 F. T. C. 209 (1921); *Geo. C. Le Genre & Sons*, 3 F. T. C. 213 (1921); *D. T. Winslow & Co.*, 3 F. T. C. 217 (1921); *T. C. Hurst & Son*, 3 F. T. C. 223 (1921); *F. V. Falck Supply Co.*, 4 F. T. C. 243 (1922); *F. G. MacFarlane*, 4 F. T. C. 292 (1922).

in the ship chandlery trade the authority of the Commission was, upon appeal, restricted by a court ruling that the sales of supplies to ships were local transactions and did not involve interstate or foreign commerce.<sup>1</sup> Apparently relying upon the "original package doctrine," the Commission has continued to issue complaints and orders against commercial bribery in the ship chandlery business under similar circumstances.<sup>2</sup> It remains to be seen whether the Commission's view of this matter will finally prevail in the courts.

The Federal Trade Commission has also attempted to treat as a species of commercial bribery, the subsidizing of salesmen of distributors as a means of encouraging them to push the sale of a particular product. The complaints first issued against this practice do not indicate whether the distributors were or were not aware of the fact that commissions were being given to their employees.<sup>3</sup> That this knowledge of the subsidy-offer was regarded as immaterial is shown by the express finding, in subsequent proceedings, that the practice was carried on with the consent of the employers.<sup>4</sup> The courts, however, have refused to uphold the condemnation of the practice on this basis.<sup>5</sup> In the *Kinney-Rome* case the circuit court of appeals declared that consumers have no special interest in the impartiality of clerks and that the public "if it has an interest in competition has such interest only in the competition between different merchants."<sup>6</sup> Both of these propositions are certainly open to question,

<sup>1</sup> *Winslow & Co., et al. v. Federal Trade Commission*, 277 Fed. 206 (1921). Application to Supreme Court for writ of certiorari denied, 258 U. S. 618 (1922). The circuit court of appeals said: "The claim that they were engaged in interstate commerce rests wholly on the fact that the commodities in which they deal are in large part transported into Virginia from other states in which they are procured. But this transportation ends when the goods reach their destination, and are placed in petitioner's warehouses in Norfolk and Newport News." With regard to foreign commerce, the court stated that the respondent's "relations with the ships cease entirely when the supplies are put on board and payment therefor is received. What becomes of them afterwards is beyond their control and in no wise their concern," p. 209.

<sup>2</sup> *Wright & Gowan Co.*, 5 F. T. C. 60 (1922); *C. T. Sweet Co.*, Complaint No. 1073, Annual Report 1924, p. 218, dismissal announced July 29, 1925.

<sup>3</sup> *Hoover Suction Sweeper Co.*, 1 F. T. C. 476 (1919); *Royal Easy Chair Co.*, 2 F. T. C. 139 (1919); *Utah Bedding Mfg. Co.*, 2 F. T. C. 185 (1919); *Carter Paint Co.*, 2 F. T. C. 181 (1919).

<sup>4</sup> *Kinney-Rome Co.*, 2 F. T. C. 442 (1920); *Shotwell Mfg. Co.*, 3 F. T. C. 25 (1920).

<sup>5</sup> *Kinney-Rome Co. v. Federal Trade Commission*, 275 Fed. 665 (1921).

<sup>6</sup> *Ibid.*, p. 669.

and the implication in the statement quoted is so contrary to established principles of public policy that there is some justification for regarding the legality of this method of sales promotion as still unsettled. It is significant that the Federal Trade Commission appears not to have acquiesced in this judicial opinion, for it has recently filed a complaint directly attacking the subsidizing of salesmen.<sup>1</sup>

In the foregoing discussion of the Commission's activity in this field, care has been taken to apply the term commercial bribery solely to the practice of giving valuable considerations to employees or agents with the intent and tendency to induce a breach of trust. This conforms to the definition formulated at the outset and to proper usage of the term "bribery," in general. There can be no element of bribery in the giving of gratuities to customers who are themselves the proprietors of the business concern the trade of which is solicited, and who are buying on their own account. There is no deceit; and breach of faith, save in a poetic sense,<sup>2</sup> is impossible.

### §11. TRADE NAME OR TRADE-MARK SIMULATION

To appropriate the good-will of a competitor by representations in any form which induce purchasers to believe that they are securing the products of such competitor is a type of commercial fraud, which, as already pointed out, gave rise to a common law action for damages.<sup>3</sup> It may not be the oldest form of unfair competition in fact, but it certainly is in law. It differs from the methods of sales cultivation previously discussed in that the injury occasioned by its use falls upon a particular competitor rather than upon competitors generally,<sup>4</sup> and this may account for its earlier condemnation. In view of the fact that the injured party may have redress in the courts in every case involving de-

<sup>1</sup> *Twinplex Sales Co.*, Complaint No. 1282, filed February 21, 1925.

<sup>2</sup> As when it is said a man may be untrue to himself.

<sup>3</sup> See Chapter II.

<sup>4</sup> A nominal exception to this statement might be pointed out in a proceeding by the Federal Trade Commission against *F. A. Maltby*, 5 F. T. C. 473 (1923). In this case the respondent, operator of a fleet of taxicabs, had advertised under some fifty names so selected that they would be listed in the telephone directory immediately preceding or following the names of competitors.

ception from imitation of products, equipment, or names, the primary question in connection with this practice is whether there is sufficient public interest to warrant administrative action by the Federal Trade Commission.

In support of the policy of the Commission in taking cognizance of cases of simulation it may be argued that while the public interest in individual instances may be slight the practice is one which cannot be tolerated in a respectable business community. It is so disruptive to business standards and so plainly an insidious method of robbery that the public, it may be said, is not justified in leaving its suppression to the chance correctives provided in the vindication of private wrongs. The common law action is expensive and tends, therefore, to be resorted to only in cases in which the simulation is clear or the damages substantial. Procedure under the Trade Commission Act affords protection to small producers having, perhaps, trade-marks of high potential value but scanty present resources for defending them.<sup>1</sup> On the other hand, it may be pointed out that frequently unfair competition of this type arises not from intentional misappropriation of another's good-will but from a casual conflict of private rights. When there is no question of good faith but simply questions of priority or of the scope and effect of private agreements, the controversy would appear to be essentially a private one, neither requiring nor justifying interference by administrative authority. It may be added that there are technical reasons for preferring the private action to the public action in simulation cases. The procedure of the Commission is not as expeditious<sup>2</sup> as an equity proceeding, in which a temporary injunction may be secured if the facts warrant relief.

<sup>1</sup> In practice, however, it appears that established concerns with large resources, fully able to bear the burdens of litigation, have been the beneficiaries of the Commission's action in this direction quite as frequently as small producers. See, for example, *The Diamond Holdfast Rubber Co.*, 4 F. T. C. 235 (1921); *Universal Battery Service Co.*, 2 F. T. C. 95 (1919); *Good Wear Tire and Tube Co.*, 2 F. T. C. 216 (1920); *Best Oil Co.*, 5 F. T. C. 92 (1922); *Bramu Packing Co.*, Complaint No. 1235, Order issued December 23, 1924. These proceedings were instituted, respectively, on behalf of the B. F. Goodrich Co., the Universal Battery Co., the Goodyear Tire and Rubber Co., the Vacuum Oil Co., and the Corn Products Refining Co.

<sup>2</sup> Although it appears that cases of this class are disposed of more promptly, after the issuance of the complaint than the general average. The first six cases involving simulation were decided in periods ranging from three to eight months, approximately.

Although in an early conference ruling the Commission stated that "where the conditions complained of involve nothing more than a question of infringing registered trademarks, a proceeding will not be instituted in the absence of important considerations of public interest,"<sup>1</sup> there has been no clear enunciation of the conditions under which this public interest would be regarded as vitally affected. Indeed, judging from the numerous cease and desist orders issued in simulation cases, in none of which does the Commission indicate the basis for its decision, but which together cover a wide range of variations of the offense, it would appear that no clear conception of the sphere of the proper exercise of its regulatory powers in this direction exists. If it does, it must be concluded that the earlier definition of policy has been abandoned,<sup>2</sup> and that the boundaries of the Commission's jurisdiction are conceived to be coextensive with the limits of the common law right of action. Altogether over sixty complaints have been issued by the Commission charging unfair competition by simulation of some feature of a competitor's business. A large proportion of these cases involve the use of a name either identical with<sup>3</sup> or closely resembling<sup>4</sup> that previously adopted by a competi-

<sup>1</sup> Annual Report, 1916, p. 59.

<sup>2</sup> This is implied in a recent announcement of changes in its rules of procedure by the Commission, which, moreover, may presage a return to the original policy. "Hereafter," states the Commission in a Press Release of March 17, 1925, "it shall be the policy of the Commission not to entertain proceedings of alleged unfair practices where the alleged violation of law is a purely private controversy redressable in the courts except where said practices substantially tend to suppress competition as affecting the public." The apparent significance of this announcement was largely negated by the issuance of an order immediately thereafter requiring the respondent, the Sandow Tool Company, to cease and desist from the practice of stamping the "trade-mark or brand 'B & S' upon the products manufactured or sold by it," this symbol being identical with that in prior use by the Browne & Sharpe Manufacturing Company. Complaint No. 1240, Order issued March 19, 1925.

<sup>3</sup> *The Electric Appliance Co.*, 2 F. T. C. 335 (1920); *Planters' Manufacturing Co.*, 4 F. T. C. 391 (1922); *Ideal Baby Shoe Co.*, Complaint No. 1146, Order issued December 3, 1924.

<sup>4</sup> *Auto Surplus Stock Co.*, 1 F. T. C. 424 (1919), simulating the name of the Surplus Auto Supply Co.; *Universal Battery Service Co.*, 2 F. T. C. 95 (1919), simulating the name of the Universal Battery Co.; *Great Republic Tire & Rubber Mfg. Co.*, 3 F. T. C. 6 (1920) simulating the name of the Republic Rubber Co.; *Hygrade Knitting Co., Inc.*, 4 F. T. C. 402 (1922), simulating the name of the Hygrade Knitting Mills, *Juvenile Shoe Co.*, 5 F. T. C. 105 (1922), simulating the name of the Juvenile Shoe Corporation of America. The order in this case was affirmed by the Circuit Court of Appeals, 289 Fed. 57 (1923) and a writ of certiorari was denied by the Supreme Court, 263 U. S. 705 (1923).

The foregoing cases are only typical of a considerable number which might be cited.



tor. Other cases relate to the simulation of a brand or trade-mark.<sup>1</sup> The Commission has also condemned the direct imitation of a competitor's product,<sup>2</sup> and even simulation of the arrangement or format of a competitor's advertising.<sup>3</sup> Moreover, jurisdiction was assumed and an order issued in one case in which the respondent and the party making application for a complaint were not competitors.<sup>4</sup> The respondent, the Liberty Paper Company, was a converter and distributor of paper bags, toilet paper, and similar paper products, while the other concern, of the same name, was a manufacturer of gummed paper known as sealing tape. The parties did not sell to the same trade, and the findings of the Commission state that neither was known to have obtained any business intended for the other. An order was issued, nevertheless, requiring the respondent to cease using the name Liberty Paper Company.

This case reveals an extension of the scope of the Commission's regulatory power over simulation practices which carries it to the farthest limits of the common law right of action. Only latterly have the courts come to recognize that the owner of a trade-mark or the user of a trade name is entitled to a remedy against the imitation of such mark or name by a concern in a non-competing line of business who attempts to trade upon the good-will attaching to the same.<sup>5</sup>

<sup>1</sup> *Block & Co.*, 1 F. T. C. 154 (1918), using the brand name "Mentholanum" in simulation of the well-known "Mentholatum"; *Malzo Coffee Co.*, 2 F. T. C. 58 (1919), using "Malzo" in simulation of "Mazo"; *Hines Underwear Co.*, 2 F. T. C. 307 (1920), using "Men's Jaeger Drawers" and similar descriptive phrases in simulation of "Dr. Jaeger's Health Underwear"; *Carbo Oil Co.*, 4 F. T. C. 102 (1921), using "Mobile A Oil" in simulation of competitor's brand "Mobiloil 'A'." Other cases of a similar stamp might be added.

<sup>2</sup> *Ware Well Co.*, 5 F. T. C. 294 (1922), in which respondent published books, similar not only in appearance, but also in substance, to the "Little Leather Library" published by a competitor, the contents in each instance being taken from expired copyrights. *Skidmore Fountain Pen Co.*, Complaint No. 961. Order issued August 20, 1924. The respondent's product was an imitation of Conklin Pens.

<sup>3</sup> *Geographical Publishing Co.*, 1 F. T. C. 235 (1918); *Ware Well Co.*, 5 F. T. C. 294 (1922).

<sup>4</sup> *Liberty Paper Co.*, 3 F. T. C. 13 (1920).

<sup>5</sup> *Aunt Jemima Mills Co. v. Rigney & Co.*, 247 Fed. 407 (1917); *Willys-Overland Co. v. Akron Overland Tire Co.*, 268 Fed. 151 (1920), affirmed 273, Fed. 674 (1921). The use of the word "Overland" to describe a brand of tires held infringement on trade name of plaintiff, a manufacturer of automobiles. *Vogue Co. v. Thompson Hudson Co.*, 300 Fed. 509 (1924). A hat manufacturer and dealer held to have simulated the trade-mark of a manufacturer of patterns. See, also, discussion and complete collection of cases in Note, 23 *Michigan Law Review*, 433 (1925).

Although there may be no deceitful diversion of patronage in such cases, there may in certain circumstances be produced serious injury to the good-will of the original user of the given trade-mark or name, and on this ground there is, in general, justification for provision of private redress.<sup>1</sup> But it is not clear that there is equal ground for extending the federal regulatory power into this more or less debatable region.

A far more important consideration bearing upon the possible delimitation of the Commission's activity in connection with the trade name simulation evil is the element of good faith. It is submitted that, if there is to be any vital significance attached to the presence or absence of a "public interest" in proceedings by the Commission under this head, the appropriate distinction would be between those cases founded upon bad faith and those arising from a bona fide dispute over private rights. With the latter the Commission as a public agency charged with the protection of the competitive process has no essential concern. Yet in several instances it has intervened in quarrels between private parties over their respective proprietary rights in a name.<sup>2</sup> The emptiness of these cases from the point of view of administrative responsibility is well exhibited by the proceedings for the protection of the Phillips brand of sausage. One Thomas W. Phillips commenced making sausage in Washington, D. C., in 1859, and the business, continued by his son,

<sup>1</sup> Some duplication of names is perhaps inevitable and occasions no deception. Outside of direct competitors it is only in the case of related lines that similarity of names may result in the misappropriation of good-will. But it would appear that not every example of similarity, which would cause confusion and the diversion of patronage among competitors, amounts to unfair competition or infringement as between concerns in related lines. Only distinctive names such as "Overland" or "Vogue" or "Peterson" would seem likely to be subject to impairment of good-will from the operations of concerns of like names or the sale of products under like brands in non-competitive, related lines. Thus, to compare the use of a non-distinctive name in a situation similar to that in the Overland case, there appears never to have arisen any question over the simultaneous use of the word "General" by the General Motors Company and the General Tire and Rubber Company.

<sup>2</sup> *Phillips Brothers & Co.*, 4 F. T. C. 297 (1922); *Phillips Genuine Sausage Co.*, F. T. C. 73 (1923); *Philadelphia Blanket Co., Inc.*, Complaint No. 1049, Order reported issued in Annual Report, 1924, pp. 182-183. The first two of these proceedings arose out of the same situation.

Attention may also be called to the case of *Universal Motor Co., et al.*, 3 F. T. C. 387 (1921), in which the Commission appears to have acted as a mediator among the three parties, all of whom asserted a bona fide claim to the name "Universal." The two respondents entered into stipulations with the complainant and they jointly requested an order in certain terms from the Commission.

ultimately became the Joseph Phillips Company. About 1891 a grandson of the founder, Thomas C. Phillips, established an independent firm for the manufacture of sausage. Upon withdrawing from this partnership some thirteen years later, Mr. Phillips conveyed to his partner the right to continue to use his name (Phillips) in connection with the sale of sausage, and this business later became known as the Phillips Genuine Sausage Company. In 1920, Thomas C. Phillips re-entered the sausage trade, in association with a brother, under the partnership name of Phillips Brothers and Company. That the intervention of the Federal Trade Commission to settle the dispute of these several parties over the right to describe their product as Phillips' Sausage, served any real public interest, which could not have been better and more conclusively served by private litigation, or clarified the law respecting unfair competition, may well be doubted. But when one of the parties, i. e., the aggressor, in trade simulation cases acts in bad faith there is presented a different situation. The public has an interest in preventing the deliberate thieving of commercial good-will, just as it has in preventing robbery of more substantial property. On this ground, the fact that a private party may have a right of action for the injury done by imitation of his trade-mark or name ought not to preclude all action by the Federal Trade Commission against this species of commercial fraud.

## CHAPTER VI

### THE REGULATION OF TRADE RELATION POLICIES

Probably in no other sphere of its activity does the Federal Trade Commission approach so closely the conception of its prime function which prevailed among those chiefly responsible for its creation as in the regulation of trade relation policies. It was originally conceived, as has been shown, as an administrative tribunal for checking predatory aggression by trusts, or monopolistic combinations, against small-scale, independent business establishments. Yet not only have the complaints filed against oppressive or exclusive tactics been relatively few in number, not exceeding ten per cent of the total number of cases docketed, but even in these instances, with only minor exceptions, the respondents against whom orders to cease and desist have issued have been small if not insignificant factors in their respective branches of trade.<sup>1</sup> To what is the meagreness of the Commission's record in dealing with this general type of unfair competition due? And what does it signify?

Two factors may be advanced as tending to effect this outcome in some degree. In the first place, it is probable that the unmistakable intention of Congress to condemn the methods of competition formerly associated with monopolization of the market and the establishment of trust supremacy was itself a deterrent to the continued employment of such methods. This, with the growing realization of the indirect economic penalties from the popular obloquy attaching to the interference by dominant concerns in the operations or affairs of their lesser rivals, may well account for the negligible citations of so-called trusts in complaints of this character. In other words, it is probable that there has been in reality but slight occasion for prosecution of combinations

<sup>1</sup> Among the exceptions may be cited: *The Fleischmann Co.*, 1 F. T. C. 119 (1918); *U. S. Hoffman Machinery Corporation*, 5 F. T. C. 439 (1923); *Armour & Co.*, 1 F. T. C. 430 (1919); *Eastman Kodak Company*, Complaint No. 977, Order issued April 18, 1924.

on this score. In the second place, the nature of the offense may possibly have a bearing upon the infrequency of the Federal Trade Commission's attention to the regulation of trade relation policies. This requires some explanation.

Broadly speaking, there are two methods of seeking survival and success in business. They are not in the nature of alternatives, however, so much as in the nature of complements. One aims to win customers for the given concern, to attract buyers of its products. The other aims to prevent sales by competing concerns. One is the positive method. The other is the negative method. The business policies founded upon the positive method of advancing trade interests are fair or unfair, legitimate or illicit, according to objective standards. They may be judged by their necessary or observed effect upon parties outside the trade, upon the purchasing public. Specifically, the issues to which price policies and sales promotion policies give rise, as has been shown, all hinge upon the existence of discrimination or deception in some form as against buyers. The unfairness to competitors is a corollary of unfairness to buyers in these cases. To judge of the fairness of trade relation policies, on the other hand, requires a direct balancing of the coordinate rights of two or more traders. There is presented a conflict of private interests, in which the public is only indirectly concerned, and in which, therefore, the effect on the public cannot serve as a criterion of fairness. The whole issue becomes one of the degree or severity of competition which can be tolerated. When does fair enterprise, by excess of zeal, become unfair "oppression," to adopt Justice McReynold's term in his classic dictum in the Gratz case?<sup>1</sup>

Malicious interference with the legitimate operations of competitors may be admitted to be unfair and unlawful. But such a statement is question-begging. It is not invariably evident when interference is malicious. Should a business man or his agents steal goods from a competitor's warehouse, or under false pretences secure such goods from a bailee, as actually happened in one case heard by the Commission,<sup>2</sup> the interference would be promptly and universally

<sup>1</sup> *Federal Trade Commission v. Gratz*, 253 U. S. 421, 427 (1920).

<sup>2</sup> *Jacob Lanski*, 2 F. T. C. 302 (1920).

condemned. But a Federal Trade Commission is not required to tell us that such a method of advancing one's trade interests is unlawful; and there is other procedure, better adapted than the Commission's for its suppression. But if a manufacturer engages a jobber to act as his exclusive distributor in a given territory, upon the reciprocal condition that the jobber shall not deal in competing products, the means in itself is certainly innocent and the decisive issue becomes one of animus. Was the contract made for the primary and direct purpose of securing more wholehearted vigorous sales representation? Or was the basic and controlling purpose to exclude competitors' products from the established channels of trade? The Commission has not, any more than did the courts under the common law, found a universal formula for determining what interference is incidental and indirect, and what is premeditated and predatory. And in the nature of things a simple criterion of fairness or unfairness in these cases, which could be mechanically applied, is out of the question. The standard rests somewhere in that nebulous and shifting concept of "fair play" between combatants. The sole guide, and it is by no means explicit, for an administrative agency undertaking the regulation of business policies concerning trade relations must be in the traditional legal standards of market conduct. To ignore the limits of private discretion in methods of dealing with competitors or distributors long sanctioned by the law, and to look simply to the consciences of the momentary custodians of public authority, in shaping administrative policy, would be to invite not only judicial rebuff but popular repudiation as well. For these reasons the Federal Trade Commission has of necessity followed a conservative course in this sphere of its jurisdiction. In attacking business practices evidencing unfair competitive aggression, the Commission has not extended the scope of coercive regulation much, if any, beyond the boundaries of what constituted actionable injury at common law. Likewise in regulating conspiracies to stifle competition *inter se* the Commission has not departed from the settled principles of law applicable to restraint of trade. It is not surprising, consequently, that in merely placing its machinery at the service of the enforcement of

old, established legal rules, the burden of the Commission's activity in this direction has not been heavy.

### §1. DISPARAGEMENT OF COMPETITORS

In one sense the most extreme form of the negative method of advancing business interests is a direct attack upon the integrity of a trade rival. False or misleading statements with respect to the reputation or financial standing of a competitor or the quality of his products have no justification in modern business practice. The fact of their falseness shows plainly that they are primarily directed to the injury of the competitor. Such a policy evinces a purpose to eliminate a troublesome competitor not by superior efficiency but by distinctly foul means. The unfairness of this method of competition is so manifest that it was recognized as illegal, in certain circumstances, already discussed, at common law. And, with possibly two exceptions, it appears that the Federal Trade Commission has not, in the several orders it has issued against disparagement, condemned what would not have been actionable under common law principles.

Approximately thirty-five complaints have been issued in which disparagement of a competitor has been charged. The number of orders to cease and desist has been much smaller, however, owing to the fact that in several cases, in which the original charge of disparagement was a minor feature of the complaint, this charge was abandoned upon the issuance of the order.<sup>1</sup> The following specific forms of disparaging attacks upon competitors have been condemned: false statements concerning the construction or effectiveness of a competitor's products,<sup>2</sup> false statements to the effect that competing products have been condemned by public authorities,<sup>3</sup> false statements regarding the credit or financial

<sup>1</sup> See, for example, Complaints No. 130-135, inclusive, as described in the Annual Report, 1918, pp. 69-70. In these well-known cases, the respondents, manufacturers and distributors of oil tanks and pumps were originally charged with "falsely representing the product of certain of their competitors to be unsatisfactory, defective, and that such would not operate. . . ." This charge is not made in the complaints as reported in connection with the orders to cease and desist, which dealt with the restrictive provisions of leases made by respondents.

<sup>2</sup> *Muenzen Specialty Co.*, 1 F. T. C. 30 (1917); *The Oakes Co.*, 3 F. T. C. 36 (1920); *Vacuum Cleaner Specialty Co.*, 3 F. T. C. 377 (1921).

<sup>3</sup> *Plunkett Chemical Co.*, 3 F. T. C. 53 (1920).

standing of competitors,<sup>1</sup> false accusations that competitors are members of a trust,<sup>2</sup> falsely characterizing competitors as "pirates" and their products as "counterfeits,"<sup>3</sup> falsely accusing distributors unwilling to handle one's product of being disloyal to the Government,<sup>4</sup> making false statements concerning the retirement of a competitor from business,<sup>5</sup> and falsely advertising that a competing product is an inferior imitation of one's own product.<sup>6</sup> It will be observed that in all of these cases it was expressly charged and found that respondents' statements regarding their competitors were either literally untrue or so calculatedly misleading as to produce a false impression. Moreover, the Commission found as a fact in each of these cases that the disparaging statements were intended to injure competitors and were calculated to have that effect. While it appears that the Commission has in no instance made a finding of specific damages, this is clearly unnecessary in a proceeding primarily in the public interest. Nevertheless, the essential elements of the common law right of action for defamation or disparagement are retained, it is evident, in this administrative action.

The really vital issue in this connection, however, is whether it may not be unfair competition to malign a business rival or depreciate his products, even though keeping strictly to the truth. There is much to be said from an ethical point of view against "throwing stones," whether or not the hurler be a resident of "a glass house." As a matter of fact it is not done by reputable firms in established lines of trade even now. There would probably be no outcry

<sup>1</sup> *Muenzen Specialty Co.*, 1 F. T. C. 30 (1917); *Gartside Iron Rust Soap Co.*, 1 F. T. C. 310 (1919); *Sunlight Creameries*, 4 F. T. C. 55 (1921); *Utah-Idaho Sugar Co.*, 6 F. T. C. 390 (1923). In the last mentioned case the question of whether interstate commerce was involved has been raised, and the issue is now before the courts.

<sup>2</sup> *Chicago Mill Works Supply Co.*, 1 F. T. C. 488 (1919); *Gordon Van-Tine Co.*, 1 F. T. C. 316 (1919).

<sup>3</sup> *Keaton Tire & Rubber Co.*, 5 F. T. C. 335 (1922).

<sup>4</sup> *Royal Cinema Corp.*, 2 F. T. C. 88 (1919).

<sup>5</sup> *St. Louis Lightning Rod Co.*, 3 F. T. C. 327 (1921).

<sup>6</sup> *U. S. Products Co.*, 7 F. T. C. 301 (1924). In this case it was found that the respondent's product was a deliberate imitation of the disparaged product, instead of *vice versa*. The justification for the order was not mitigated by the fact that the respondent was proved to have forged letters as a basis for a request to the Federal Trade Commission to institute proceedings against a competing manufacturer.



from conservative business quarters, consequently, if disparagement or depreciation of competitors were completely and absolutely outlawed. On the other hand, while it may not be a responsibility of a manufacturer to educate the public in the deficiencies of substitute products which are detracting from the demand for his own product, that is certainly his privilege. And if, to take a simple example, dairies may compare the merits of butter and oleomargarine, with emphasis on the disadvantages of the latter, may not chicken farmers point out the superiority of fresh eggs to storage eggs? Once this privilege of depreciating competing products by publishing verifiable facts about them is granted, the extension of the privilege to true statements concerning the products or business reputation of a particular rival firm might appear difficult to prevent. The identification may be assured by devious means not involving the naming of the given competitor. But the courts have never found themselves powerless to pierce subterfuges of this order, and there is no reason to believe they would present insurmountable administrative difficulties to the Federal Trade Commission. There do not appear, in short, to be any serious practical objections to a modification of policy which would make disparagement of competitors or depreciation of their products illegal *per se*, provided always that the attack is definitely directed against particular competitors. Where, however, the attack is general in character, as upon a different form of trade organization or upon all competing products of a class, it would seem to be sufficient protection to competitors if only false and misleading statements of a deprecatory character were condemned.<sup>1</sup>

There is not much likelihood for the present that higher standards of business ethics, such as this rule would embody, are to be imposed by coercive regulation. In only a single proceeding,<sup>2</sup> so far as has been ascertained, has the Federal Trade Commission given any indication that it might be feasible to deal with disparagement of competitors more rigorously under Section 5 of the Trade Commission Act

<sup>1</sup> It was upon this basis that a recent order was issued against the *Wisconsin Cooperative Creamery Ass'n.* Complaint No. 1080. Advance Sheets, June 9, 1925.

<sup>2</sup> *Wayne Oil Tank & Pump Co.*, 1 F. T. C. 259 (1918).

than it was under the common law. The respondent in one of the early cases had circulated copies of a newspaper item showing that a certain competitor had been convicted of violating the Sherman Anti-Trust Act. The Commission did not find that this press dispatch was untrue, nor did it appear that in giving this news item wide publicity the respondent had accompanied it by any derogatory insinuations or comments. Nevertheless an order was issued in the most sweeping terms forbidding the circulation of this, or similar, information.<sup>1</sup>

No appeal was taken from this order, so that what the judicial view of it might have been can only be speculated upon. It is significant, however, that since this early case the Commission appears to have instituted no proceedings of this character in which the falsity of the alleged disparaging statements was not explicitly charged.

What the attitude of the courts might be towards an attempt to bring within the scope of the prohibition of unfair methods of competition all derogatory statements about competitors, regardless of their truth or falsity, is perhaps indicated by the judicial review of an order by the Commission in a subsequent case.<sup>2</sup> The respondent, it appeared, had caused chemical analyses to be made of an antiseptic made by a competing manufacturer. The unfavorable results of these analyses were communicated to four large customers of the competitor, accompanied by such statements as that, "It is our opinion that its use on the human body would be attended with great danger." The Commission did not specifically find that the analyses circulated by respondent were inaccurate, but it did find that the analyses in conjunction with the accompanying statements were deceptive and misleading and resulted in loss of trade

<sup>1</sup> *Ibid.*, p. 270. In paragraph 2 of the order the respondents were directed to cease: "Publishing or circulating . . . a printed clipping or circular which is a copy of a news item which appeared in the Indianapolis News . . . wherein it is reported . . . that a certain competitor of respondent had been found guilty of engaging in a combination in violation of the Sherman Anti-Trust Act . . . ; or publishing or circulating in a similar manner any printed clipping or circular similar in form, purpose, or effect, regarding any competitor of the respondent."

<sup>2</sup> *John Bene & Sons Co. v. Federal Trade Commission*, 299 Fed. 468 (1924).

to the competitor.<sup>1</sup> In reviewing the Commission's ruling the circuit court of appeals subjected the testimony and the findings in this case to a critical examination, and concluded that, while the Commission might have been justified in finding that respondents' disparaging representations were misleading, yet the Commission exceeded its powers in holding that respondents' action constituted unfair competition. The court declared that the Commission had omitted to find as a fact, what the testimony clearly revealed, that the competitor's product was misrepresented by the producer himself. On this ground the court annulled the order to cease and desist. Since it appears, thus, that in the judicial view it is not unfair competition to exaggerate actual defects or faults in a competitor's products, if this is but an offset to misrepresentation of his own products by the competing producer, it may perhaps be deduced that it would not be regarded as unfair competition to call attention in measured terms to defects or faults in competing products even in the absence of this provocation.

## §2. HARASSING TACTICS

The negative method of advancing competitive interests, i. e., the method of interfering with trade rivals, may be carried on indirectly as well as directly. In this section will be briefly surveyed several of the indirect and more or less surreptitious practices, which illustrate the substance and the scope of this branch of trade regulation. These practices appear not to be confined to any particular type or size of industrial enterprise. They tend, perhaps, to occur more commonly under the severe pressure which is exerted upon those occupying an unfavorable position in trade, but they also spring occasionally from an excess of zeal, on the part of vigorous and enterprising firms, in struggling for supremacy.

The activity of the Federal Trade Commission in reference to the use of harassing tactics against competitors has not been as extensive or as striking, either relatively or absolutely, as the debates leading to the establishment of the

<sup>1</sup> *John Bene & Sons Co.*, 5 F. T. C. 314 (1922).

Commission might indicate was anticipated.<sup>1</sup> In part this may be due to a decline in the employment of predatory practices of this sort and a corresponding elevation of business standards. But it appears that it may also be traceable to difficulties of a technical character connected with the provision of satisfactory proof in such cases. The essential unfairness of some methods of harassing competitors is clear. In particular such practices as mutilating, tampering with, or adulterating a competitor's product,<sup>2</sup> removing the advertising display boards distributed by a competitor,<sup>3</sup> or purposely causing collisions with the motor trucks of a competitor,<sup>4</sup> call for no detailed discussion. The invasion of competitors' rights is so palpable that the conclusion that these tactics tend to hamper free competition is unescapable. But there are other practices involving interference with the business of competitors which are in the nature merely of an intensification of ordinary and legitimate competitive methods. In the determination of the legal status of alleged unfair conduct in many cases of this character the motive of the act, rather than its substantive nature, becomes the decisive factor. It is a question, frequently, of whether or not the act was done with the wrongful intention of injuring a competitor. When, for example, a dealer-customer is prevailed upon to rescind a contract with a given manufacturer, or to cease purchasing of him, and to give his entire trade to the intruding competitor, has the latter deliberately wronged his rival or only sought his own profit? This can seldom be determined with much assurance. It is noteworthy, as bearing upon the Commission's activity in this field, that a relatively large number of complaints have been dismissed, and frequently on the ground, according to the terse official explanation of "failure of proof" or "evidence not sufficient."<sup>5</sup>

<sup>1</sup> Approximately forty-five complaints have been issued in which the major charge appears to have been some type of harassing competition. In a number of cases such methods have been alleged as supplementary to other practices.

<sup>2</sup> *Essex Varnish Co.*, 1 F. T. C. 138 (1918); *Muenzen Specialty Co.*, 1 F. T. C. 30 (1917); *Vacuum Cleaner Specialty Co.*, 3 F. T. C. 377 (1921).

<sup>3</sup> *Keaton Tire & Rubber Co.*, 5 F. T. C. 335 (1922).

<sup>4</sup> *American Agricultural Chemical Co.*, 1 F. T. C. 226 (1918).

<sup>5</sup> Among the cases dismissed may be noted the following: *Coca Cola Co.*, 2 F. T. C. 461 (1919) (espionage); *Darling & Co.*, 4 F. T. C. 483 (1921) (espionage);

(a) *Espionage*

Within certain limits inquiry concerning the affairs of trade competitors is certainly legitimate. There is no economic objection to a business man keeping informed about the general financial position, the sales program, or the nature and extent of the research work, of each of his competitors so far as these can be ascertained from observation or from published statements. But in respect to each of these matters there are detailed facts which business concerns do not generally make known or care to have known outside of their own organizations. The maturities of current obligations to banks, the terms and volume of particular orders or sales, the progress of technical experiments—these are matters about which, unless and until they are publicly announced, competitors are not entitled or warranted to seek information. When, therefore, a firm undertakes to secure detailed facts of this nature about the business of its competitors it must ordinarily proceed by stealth. This affords a fairly reliable index of the limits within which the common business function of assembling and utilizing information about trade conditions may be cultivated without encroaching upon the privacy and security of others. The offense of espionage, in sum, is to be tested not primarily by the character of the information sought or obtained, and not even by the attitude of the party, whose affairs are the subject of inquiry, towards disclosure of the given facts. The real test of what constitutes espionage is afforded by the presence or absence of duplicity or bad faith in the means employed to acquire the particular information.

This analysis is borne out by the proceedings thus far instituted by the Federal Trade Commission to suppress this evil. In several cases the Commission has condemned

*American Tank & Pump Co.*, 2 F. T. C. 462 (1919) (inducing breach of contract). *Tokheim Mfg. Co.*, 2 F. T. C. 463 (1919) (*idem*, and enticing employees); *Guarantee Liquid Measure Co.*, 2 F. T. C. 463 (1919) (*idem*); *U. S. Food Products Corp.*, 3 F. T. C. 435 (1920) (enticing employees); *Ironite Co.*, 3 F. T. C. 436 (1920) (threats of litigation); *Meccano Co.*, 2 F. T. C. 461 (1919) (*idem*); *National Bridge Co.*, 3 F. T. C. 437 (1920) (*idem*); *Niles Normalizing Machine Co.*, 2 F. T. C. 461 (1919) (*idem*); *American Chiclo Co.*, 1 F. T. C. 539 (1919) (*idem*); *Gilbert & Barker Mfg. Co.*, 2 F. T. C. 462 (1919) (inducing breach of contract); *The Shredded Wheat Co.*, 2 F. T. C. 464 (1919) (espionage, threats of litigation); *Dalby & Hardwick*, 4 F. T. C. 483 (1921) (including vexatious demands); *Minerals Separation, Ltd.*, Complaint No. 215; Dismissed April 11, 1923. (Espionage, intimidation, threats of litigation.)

the employment of detectives to spy upon a rival, and the bribing of a competitor's employees to obtain confidential information.<sup>1</sup> Whether the purpose of the procurement of information by such means is primarily injury to the competitor or not, these tactics tend in the long run to hamper and discourage competition. They reduce the conduct of business to the level of trickery. From the social point of view they are, therefore, as pernicious as they are clearly unfair from the point of view of the particular competitor.

*(b) Inducing Breach of Contract*

It has never been seriously contended that there is any unfairness in offering to sell one's products in the ordinary course of trade to everyone who may deal in or consume such products, even though each particular transaction completed may tend to curtail by so much the potential demand for competitors' goods. This is but an aspect of the inevitable harshness not only of a competitive economic system but of life itself. Nor should the existence of contractual relations between a prospective customer and a competitor constitute a bar to commercial intercourse. If an offer is made in good faith, primarily for one's own profit, the fact that it may incidentally result in the breach of an executory contract between a competitor and the customer to the former's damage would not seem adequate ground for regarding it as an offense against public law. And yet if the jurisdiction of the Federal Trade Commission, in this particular, were to be made coterminous with the grounds for a private right of action for procurement of breach of contract, the conclusion of a transaction under these circumstances might justify the issuance of an administrative order. For at common law, as already shown, the negotiation of a contract with another, e. g., a sale to a dealer customer, with the knowledge that its performance will bring about the breach of an existing contract was, in most American courts, ground for recovery of damages by the injured competitor.<sup>2</sup>

<sup>1</sup> *Botsford Lumber Co., et al.*, 1 F. T. C. 60 (1918); *American Agricultural Chemical Co.*, 1 F. T. C. 226 (1918); *Allen Sales Service*, 1 F. T. C. 459 (1919); *The Oakes Co.*, 3 F. T. C. 36 (1920); *United Rendering Co.*, 3 F. T. C. 284 (1921); *U. S. Hoffman Machinery Corp.*, 5 F. T. C. 439 (1923).

<sup>2</sup> See Chapter II, *supra*.

As a basis for action by the Federal Trade Commission something more than mere knowledge of an existing contract and intention to do that which will, in ordinary course, bring about its breach would seem to be essential. For the public interest, which is the fundamental guide to Commission procedure, lies not so much in the preservation of the contract, as in the prevention of unfair business conduct. And the common law liability for interfering in the execution of valid contracts might well be somewhat more extensive than the responsibility not to employ unfair methods of competition, as applied to the solicitation of business from customers of competitors. The existence of a legitimate trade interest in expanding one's sales should supply, so far as the unfairness of the conduct from the public point of view is concerned, that "just cause or excuse" which the common law requires, but which it does not, in general, recognize to be provided by competitive interest. But this should be held to constitute justification, it must at once be added, only under the circumstances set forth, namely, the pursuit in ordinary course of one's immediate private profit and advantage. When unlawful means are used to induce breach of contract, or when the interference serves no positive competitive interest of the trader responsible for the contract cancellation, a different case is presented. In short it would seem that evidence of ill-will, in the sense of a primary intention to thwart or cause loss to a competitor, should be recognized as an essential element in the grounds for procedure by the Federal Trade Commission in this class of cases.

The record of the Federal Trade Commission thus far in dealing with procurement of breach of contract does not indicate that a different policy from the foregoing is being followed. There has been no case in which the Commission has gone so far as have the courts in some common law actions in condemning the interruption of contract relations which results incidentally from the advancement of one's own business interests.<sup>1</sup> In one instance the Commission held,

<sup>1</sup> A possible exception to this general statement may be the case against the *Wayne Oil Tank & Pump Co.*, 1 F. T. C. 259 (1918). From the official report of this proceeding one would be led to believe that the respondent had pursued a definite and deliberate policy of interfering with the installation of competitors'

quite properly, that requesting and inducing third parties to break their contracts with competitors, when such action has no direct relation to the procurement of any profit or advantage to the person soliciting the cancellation, is unfair and unlawful.<sup>1</sup> Adverse orders have been issued in two cases, moreover, in which it appeared the respondents had offered special inducements to buyers to rescind their contracts for the purchase of competing equipment and replace same by the equipment manufactured by the respondents.<sup>2</sup> Among such inducements were offers to indemnify customers for any judgments rendered against them on account of cancellation of contracts with respondents' competitors, and offers to credit installment payments made upon purchases from respondents' competitors toward the price of respondents' products. In these cases malice is evident and the corrective action of the Commission is undoubtedly well-founded. So long as jurisdiction is not assumed beyond the range here indicated, procedure by the Commission to prevent interference in existing contract relations may be expected, upon occasion, to have judicial sanction.

From another angle, it appears that administrative regulation in this field may effectively add to the protection accorded by the common law. In common law suits for inducing breach of contract it has always been necessary to show injury.<sup>3</sup> No recovery was possible if no damage resulted. Under the Federal Trade Commission Act, on the

service station equipment "by divers means and methods." It is not even mentioned whether in seeking the rescission of contracts for competitors' equipment the substitution of its own product was encouraged. But the agreed stipulation upon which this case was heard and decided presents quite a different aspect of the facts. From the stipulation it appeared that the procurement of breach of contracts for the purchase of competitors' equipment had taken place only in isolated instances, and against explicit and repeated instructions of the respondent to its managers and agents. For a further discussion of the discrepancy between the Commission's official "Findings of Facts" and the agreed stipulation in this case, see G. C. Henderson, "The Federal Trade Commission," New Haven, 1924, pp. 141-142.

<sup>1</sup> *Stanley Booking Corp.*, 1 F. T. C. 212 (1918). In this case respondent was found to have procured, by means not stated, the "cancellation of contracts for the exhibition of certain moving-picture films made and entered into by and between certain of its competitors similarly engaged and the producers of moving-picture films." It is not related and there is no basis for assuming, that this enabled respondent to secure films which it could not otherwise have obtained.

<sup>2</sup> *U. S. Hoffman Machinery Corp.*, 5 F. T. C. 439 (1923); *Prosperity Co., Inc.*, 6 F. T. C. 290 (1923).

<sup>3</sup> See Chapter II, *supra*.



other hand, as interpreted, it is unnecessary to prove that the attempts were successful in causing the cancellation of a single contract.<sup>1</sup> The unfairness which the law condemns resides in the adoption of the policy of interfering in competitors' contract relations, and the accomplishment of the intended result is merely an aggravation of the offense. From still another viewpoint, it may be observed that administrative regulation is capable of providing protection against interference with several isolated contracts, which singly may involve sums too small to justify private legal action against the unfair aggressor or even suits for breach of contract. The cases of this nature thus far prosecuted by the Commission afford no clear illustration of these advantages of its procedure, however.

(c) *Enticement of Employees*

Interference with the employment relations of a competitor stands on a similar footing with inducement of breach of commercial contracts. Except for the difference in subject matter there is no essential ground for distinguishing malicious interference in the one relation from the other. Competition for services and competition for patronage are merely different phases of competitive business rivalry. This is recognized in the law, which regards any agreement to abstain from offering inducements which would cause the employees of a competitor to leave his employ, i. e., to hire them away from him, as in the nature of a conspiracy to keep down wages. It is as unlawful as an agreement not to offer goods to buyers below a certain price, which is the clearest example of a conspiracy in restraint of trade. Contrariwise, unfairness arises when special offers are made to particular employees, not primarily in order to secure their services but in order to injure their actual employer. The injury may be accomplished either by depriving the competitor of valuable services without adequate notice or by

<sup>1</sup> An examination of the records discloses that with one exception all of the complaints against this species of unfair competition have charged not only the inducing but the "attempt to induce or procure" breach of contracts, and presumably proof of the latter would be sufficient to support an order, else there would be no reason for thus framing the complaint. The exception noted is: *Stanley Booking Corp.*, 1 F. T. C. 212 (1918).

securing through trusted employees confidential information concerning his business. Here again, as in respect to espionage and inducing breach of contract, the unfairness of the conduct subject to complaint does not ordinarily reside in the substance or form of what is done. Acts which are by themselves quite innocent become vicious when prompted by predatory design. In any given case the enticement of employees may be properly condemned if it can be shown that the prime purpose served was the injury of a competitor. But as with other types of harassing tactics the determination of the existence of this improper motive is attended with great difficulty, and can be deduced as a rule only presumptively from the totality of surrounding circumstances.

In the three cases involving enticement of employees in which orders to cease and desist have been issued, the Federal Trade Commission appears to have recognized that there is no escape from this difficulty, which comes down from the common law.<sup>1</sup> Thus, in one case it was charged that respondent had systematically and on a large scale induced employees of one of its competitors to leave their employment, when respondent had no occasion for the services of many of such employees.<sup>2</sup> The findings state that respondent had "maliciously enticed away employees of said competitor"; and furthermore that respondent had "acquired information of trade secrets and business confidences of a competitor through and by a person formerly employed in a confidential capacity by said competitor, but now employed by the respondent."<sup>3</sup> In another case, decided upon an agreed stipulation of facts, it appeared that the respondent had sought and obtained the services of salesmen who at the time were in the employ of a competitor, for the purpose of injuring said competitor.<sup>4</sup> The order to cease and desist in this case, however, seems to exceed what was required for the protection of the legitimate interests of competitors. In unqualified terms it restrained respondent

<sup>1</sup> *Standard Car Equipment Co.*, 1 F. T. C. 144 (1918); *Wayne Oil Tank & Pump Co.*, 1 F. T. C. 259 (1918); *Warthington Creamery & Produce Co.*, Complaint No. 1087, Order issued March, 1925.

<sup>2</sup> *Standard Car Equipment Co.*, 1 F. T. C. 144 (1918).

<sup>3</sup> *Ibid.*, p. 148.

<sup>4</sup> *Wayne Oil Tank & Pump Co.*, 1 F. T. C. 259 (1918).

from "employing or attempting to employ . . . any sales agent or agents or other employees of any such competitors." This comes dangerously near to forbidding under the Federal Trade Commission Act what is encouraged by the Sherman Act.

*(d) Threatening Litigation*

Attempting to intimidate a competitor by threats of law suits is usually associated with unsettled disputes over patent claims. Such controversies offer special opportunities for abuse. They almost invariably involve intricate questions of law and fact and their outcome is, therefore, quite uncertain. They afford, thus, convenient cover for disingenuousness. Moreover, the fact that such litigation can readily be stretched out over a considerable period adds to its effectiveness as a means of annoying or harassing a competitor. Since the precise limits of a patent claim can seldom be determined outside the courts, and since the chances of simple mistake in bringing charges of infringement are so great, it may be stated that, as a general rule, until a pending controversy is finally adjudicated, it would be futile to accuse a challenging patent owner of bad faith. When, however, threats are made but legal proceedings are not instituted or when instituted are not brought to trial, it may be inferred that the intimidation of a competitor rather than prevention of infringement is sought.

The difficulties surrounding the administrative regulation of this species of sharp business practice are well illustrated in the single case of this kind which has been reviewed in the courts. It appeared that one Dr. Herman Heuser, the respondent, had a valid patent on a process for manufacturing non-alcoholic beer, which he claimed was infringed by another patented process controlled by the Baltimore Process Company.<sup>1</sup> In June and September, 1921, Heuser wrote to numerous persons and firms advising them that should they exercise their privileges as licensees of the Baltimore Company they were liable to suit for infringement of his patent. In December, 1922, the complaint was issued by the Federal Trade Commission, whereupon (in January and February,

<sup>1</sup> *Dr. Herman Heuser*, 7 F. T. C. 107 (1923).

1923) the respondent Heuser, filed suits against two of the concerns previously warned.<sup>1</sup> On the basis of these facts the Commission subsequently issued its order to cease and desist. Upon appeal to the courts this order was vacated on the ground that bad faith was essential, and that the Commission had failed specifically to find such bad faith.<sup>2</sup> On the merits of the case, some support for the Commission's order might be found in the fact that respondent had evidently taken no action against the Baltimore Process Company as the alleged primary infringer. The court, however, going beyond the mere technical point of the insufficiency of the findings, stated that in its opinion the Commission was "right in failing to find bad faith." In support of this view, it pointed out several circumstances, including the fact that very few letters threatening suit were sent, which tended to establish the respondent's sincerity of purpose. It should be manifest that proceedings of this nature must frequently encounter delicate issues of fact, better suited to determination by the judicial process than by the more blunt and dynamic administrative process.

Other cases involving threats of infringement suits have shown clearly enough, nevertheless, that there is need for the repression of this practice as an unfair competitive method. When no patent rights exist as a basis for warnings against infringement, it is obvious that threats of litigation are unfair.<sup>3</sup> Though such false claims as to patent infringement might not be expected to intimidate an alleged infringing manufacturer, since he can readily ascertain their falsity and ordinarily has a sufficient interest to do so, the gesture may be effective in frightening dealer-customers of such competing manufacturer and thereby injuring his trade.<sup>4</sup> Again, making vague and indefinite threats not

<sup>1</sup> It may be noted that both of the companies sued had previously answered the respondent's letters to the effect that they were no longer using the disputed process.

<sup>2</sup> *Herman Heuser v. Federal Trade Commission*, 4 Fed. (2d), 632 (1925).

<sup>3</sup> *Gartside Iron Rust Soap Co.*, 1 F. T. C. 310 (1919); *Eskey Harris Feature Film Co.*, 5 F. T. C. 219 (1922).

<sup>4</sup> This was the situation disclosed in two cases in the drug and chemical trade, in which adverse orders were issued. *Sunbeam Chemical Co., Inc.*, 3 F. T. C. 365 (1921), and *Albany Chemical Co.*, 3 F. T. C. 369 (1921). In the first of these cases the claim to alleged infringement was backed up by the false statement that respondent had secured an injunction against the competing manufacturer. In the

based upon any meritorious patent claim, and known at the time not to have any such foundation, shows an evident lack of good faith well justifying action by the Commission.<sup>1</sup> Likewise, the attempt to intimidate dealers handling competitor's products by sweeping allegations of infringement in excess of definitely adjudicated rights of the respondent, indicates bad faith, and brings the practice within the purview of the regulatory power of the Federal Trade Commission.<sup>2</sup>

It appears that in only a few instances has the Commission definitely and explicitly found that there was a want of good faith on the part of the respondents in proceedings of this character.<sup>3</sup> These were all early cases, and it may be expected that since the reversal suffered in the recent Heuser appeal the Commission will take pains henceforth to establish this essential element before issuing orders to cease and desist from this practice. This is not to imply that in the other cases mentioned above there was not actually unfair competition and a violation of the Federal Trade Commission Act. But it is to insist, as the court insisted in the Heuser case, that unless warnings against infringement or threats of litigation are made without a reasonably founded belief in the validity of the legal claim they assert and a genuine intention to defend it, they do not constitute an unfair method of competition. The competitive process

second, which involved the right to use the trade name "aspirin," the respondent's claim was so meretricious, being backed by certificates of registration obtained under false pretenses from numerous states, that serious injury might have been suffered by the competing manufacturer, who had built up a considerable demand for his product under this name, had the respondent's campaign of intimidation among jobbers and druggists been allowed to continue. The shadowy nature of respondent's claim was evidenced by the conspicuous absence of assertion of its rights against the alleged infringing competitor.

<sup>1</sup> *Nulomaline Co.*, 1 F. T. C. 400 (1919), in which the respondent was found to have claimed the exclusive right to manufacture invert sugar sirup, although the product had been manufactured by other methods for many years.

<sup>2</sup> *Champion Blower & Forge Co.*, 3 F. T. C. 137 (1920). The findings of facts in this case brought out that respondent had declined to reply to an inquiry as to what products of the competitor were infringements. *Brown Portable Conveying Machinery Co.*, 2 F. T. C. 143 (1919), in which it appeared from an earlier and unsuccessful proceeding respondent's patents were of questionable scope, but respondent's agents falsely represented to customers that respondent had or was about to institute an infringement suit against a certain competitor.

<sup>3</sup> *Chicago Lino-Table Co.*, 1 F. T. C. 110 (1918); *Gartside Iron Rust Soap Co.*, 1 F. T. C. 310 (1919); *National Binding Machine Co.*, 1 F. T. C. 44 (1917).

cannot be preserved by denying to manufacturers and traders the right to contend for, and protest against invasion of, privileges which have been acquired and exercised in good faith.

(e) *Writing for Catalogues or Estimates*

For a business concern deliberately to plan and adopt measures looking to the imposition of expense upon a competitor, without prospect of its own gain and solely to the end of injuring such competitor, is manifestly unfair and socially wasteful. It is in fact so indefensible that it seldom, if ever, occurs among rival concerns similarly organized and conducting their business by similar means. But the bitterness engendered by the conflict between the traditional system of distribution and the newer forms of mercantile enterprise has led to a peculiar abuse of this nature. Mail-order houses dealing with widely scattered patrons and having no facilities for display of merchandise have to rely upon a free distribution of catalogues, samples, estimates, and the like, to many unknown persons for the development and effective cultivation of contacts with potential buyers. The expense of distributing such advertising material is frequently very great. Taking advantage of the vulnerability of mail-order houses in this respect, "regular" dealers have sometimes encouraged fictitious requests for catalogues or estimates. When there is no intention to patronize the mail-order concern, the application for free literature or services is a form of personal dishonesty most deserving of condemnation. When an organized effort is made to persuade others to adopt a like course, the unfairness becomes more than a personal delinquency and is properly subject to restraint by the Federal Trade Commission.

In three early cases the Commission assailed this method of harassing distant competitors.<sup>1</sup> All of these related to the lumber trade, but in a later case, a local Chamber of Commerce was the respondent and its method of protecting the interests of resident merchants by arranging with a motion picture theater to accept the catalogues of divers

<sup>1</sup> *Batsford Lumber Co.*, 1 F. T. C. 60 (1918); *St. Lawrence Lumber Co.*, 1 F. T. C. 325 (1919); *J. H. Patterson Co.*, 1 F. T. C. 363 (1919).

mail-order concerns in lieu of admission fee was condemned.<sup>1</sup> Such tactics seem clearly within the scope of administrative regulation.

### §3. BOGUS INDEPENDENTS

Prior to the enactment of the 1914 legislation there had been considerable agitation against the employment of bogus independents by trusts. The chief ground for the disapproval of the policy of conducting business operations through subsidiaries with concealed ownership appears to have been that it enabled a large concern to carry on harassing attacks upon competitors with comparative impunity.<sup>2</sup> Local price-cutting campaigns could be engineered without bringing discredit on the trust, so long as the real identity of the bogus independent remained undetected.<sup>3</sup> Likewise this device served as a spying system for obtaining information of a confidential character regarding the activities and designs of competitors.<sup>4</sup> But while the use of bogus independents was generally condemned for these reasons, no specific prohibition of the device was provided in the Clayton Act. Apparently the view was that, as the evils for which subsidiaries of undisclosed ownership could serve as an instrument were declared unlawful, the policy of operating through such subsidiaries could be allowed to stand in the absence of abuse. In defense of this view, it may be observed that secrecy regarding the ownership of a subsidiary, no more than secrecy about the distribution of stock-holding in any single corporation, is not in itself unethical or unfair. It is no part of the rights or privileges of the trading community or of the consuming public to be informed of the ownership personnel of business corporations. It certainly becomes immoral, however, if there is deceitful misrepresentation of an actual relationship between given enterprises, as, for example, by a public denial of some rumor of this connection; and such

<sup>1</sup> *Chamber of Commerce of Missoula*, 5 F. T. C. 451 (1923).

<sup>2</sup> See W. H. S. Stevens, "Unfair Competition," *op. cit.*, pp. 19-39.

<sup>3</sup> Illustrations of such use of bogus independents may be found in: "Report of Commissioner of Corporations on the Tobacco Industry" (1909), Part I, p. 110; *U. S. v. Corn Products Refining Co.*, 234 Fed. 964, 983-4 (1916); *U. S. v. American Can Co.*, 230 Fed. 859, 887 (1916).

<sup>4</sup> See *Ware Kramer Tobacco Co. v. American Tobacco Co.*, 180 Fed. 160, 167-8 (1910).

misrepresentation may conceivably become legally unfair under certain circumstances.

The proposition that a business enterprise may appear in the markets only under a single identity is economically and legally indefensible. In the first place, what constitutes such identity as requires the acknowledgment of an inter-relationship between two business concerns? Is partial ownership, effective control, absolute control, or complete ownership of one by the other to constitute such identity of interest as it is unfair not to disclose? Practically, it may be pointed out, there may be a complete ownership of one concern by the other, but they may be administered by separate managements and operate in distinct fields, as when a magazine publisher owns a book-paper mill. Under these circumstances it is difficult to understand how the failure to announce this relationship could in any way prejudice the legitimate interests of competitors of the publishing house.

In respect to more basic considerations, what objection can be raised to an appeal for patronage upon a single product or line of products under two different names, either in the same or in different markets? It is not a common practice, primarily for the reason that the reputation of a business firm ordinarily helps rather than hinders the disposal of its products. The identity of the producer serves to introduce favorably new products to old customers or old products to new customers. But if, for any reason, this condition does not obtain there does not seem to be ground for denying the privilege of seeking to develop good-will for two or more enterprises at the same time. Perhaps the "manufacture" of trade good-will may be made more profitable in this way. In any case, unless one or more of the really identified but nominally independent concerns is used for the conduct of business by methods in themselves unfair and unlawful, the failure to announce their relationship is not deceit but ordinary privacy.

From the very few cases involving the use of bogus independents which have been prosecuted by the Federal Trade Commission, it appears that the policy heretofore followed has been diametrically opposed to that suggested by the



foregoing analysis. Four orders to cease and desist have been issued, covering this practice,<sup>1</sup> three have been dismissed,<sup>2</sup> and one remains pending.<sup>3</sup> As a rule, it may be noted, the allegation of this practice has evidently been subordinated to other issues, but in only a single instance does it appear that the use of a bogus independent was connected with, in the sense of being a medium for, other alleged unfair methods of operation. In the Fleischmann case, the Berry Seed case, and the Lightning Rod case it appeared that the purpose of conducting the subsidiaries as independent concerns was to secure patronage from sources which for some reason were prejudiced against or antagonistic to the respondent.<sup>4</sup> For example, in the Berry case the respondent merely utilized the name "Standard Seed Company" in the wholesale branch of its business.<sup>5</sup> This evidently was to obviate the drawback of its status as a retail mail-order house in dealing with merchants.<sup>6</sup> But that there is no unfair competition in this has already been shown in the discussion of misrepresentation of trade status. The protection by public authority to which competitors and customers are entitled is protection in the vital terms of commercial bargains and the vital attributes of business property. The agency of federal trade regulation has no mandate for the protection of the prejudices, whims, suspicions, and idle fancies of everyone engaged in the transaction of business.

<sup>1</sup> *Fleischmann Co.*, 1 F. T. C. 119 (1918); *Armour & Co. and Farmers' Cooperative Fertilizer Co.*, 1 F. T. C. 430 (1919); *A. A. Berry Seed Co.*, 2 F. T. C. 427 (1920); *St. Louis Lightning Rod Co.*, 3 F. T. C. 327 (1921). In *Eastman Kodak Co.*, Complaint No. 977, Order issued April 18, 1924, it appeared, according to the findings of facts, that there had been for a time concealed ownership by the respondent of certain film laboratories, but this control had been publicly announced prior to the issuance of the complaint. The order is silent regarding this practice.

<sup>2</sup> *Atlantic Ice & Coal Co.*, 1 F. T. C. 539 (1918); *U. S. Food Products Corp.*, 3 F. T. C. 435 (1920); *White Sewing Machine Co.*, 4 F. T. C. 483 (1921).

<sup>3</sup> *Armour & Co.*, Complaint No. 163, Annual Report, 1924, p. 195. This case is in suspense pending close of Dockets 455 and 531.

<sup>4</sup> In each of these cases there were present other issues, not pertinent to the present discussion.

<sup>5</sup> The fact that the Standard Company appears to have misrepresented the quality of its seed, might make of the company itself a "fighting instrument," worthy of suppression; but the Commission did not treat these "offenses" as mutually dependent. They were regarded as separable and distinct elements of the respondent's policy.

<sup>6</sup> The complaint was, in general terms, that purchasers "are fraudulently induced to trade unknowingly with the respondent through the instrumentality" of the subsidiary.

In the proceedings against Armour and Company there is nothing to indicate that the respondent's purpose was to employ the subsidiary as a means of predatory attack upon competitors. The name Farmers' Cooperative Fertilizer Company might perhaps mislead customers, but in the absence of a uniform judicial or legislative definition of what constitutes a cooperative enterprise and regulation of the use of the term, it is submitted that the action of the respondent was not so far unfair as to be unlawful. This conclusion is confirmed by the evidence tending to show that respondent's selection of the name of the subsidiary was quite casual and any deception caused quite inadvertent. It appeared that the Armour Fertilizer Works had purchased outright the plant and good-will of the Farmers' Cooperative Guano Company, and had caused to be organized the Farmer's Cooperative Fertilizer Company to take over these properties. The respondent continued to operate the business under this name for upwards of five years prior to the issuance of the complaint without engaging in any unfair or predatory business practice, so far as the Commission ascertained. Moreover, upon being informed of the contemplated action of the Commission the respondent voluntarily added the words "Armour Owned" to the signature of the Farmers' Cooperative Fertilizer Company upon all equipment, advertisements, letter-heads, and the like. Under these circumstances it is difficult to understand how the conduct of the respondent constituted unfair competition in any just sense.

It is sometimes suggested that a large, perhaps potentially monopolistic concern, stands in a different relation to the requirements of the law respecting the standards of competitive conduct than its small, independent rivals. It is said they must avoid even the appearance of evil, and that the possession of instrumentalities of oppression by them may be taken as *prima facie* evidence of the exercise of oppression. On this ground there might be some justification for an order requiring Armour and Company not to do business in any circumstances under another name. But it is submitted that there is no basis, either in law or in justice, for imposing a "double standard" in respect to the legitimacy or fairness of competitive conduct. What it is equitable to

permit a small concern to do, it is equitable to permit a large concern to do. There is nothing vicious in bigness *per se*. And to penalize bigness, because of size alone, would certainly be to invite economic decay. It is to be hoped, at least, that the Commission based its action in this case on no such fallacious premise. Beyond this, there is need of a definite recognition that concealment of ownership of subsidiary corporations is not synonymous with the operation of bogus independents, and is not in itself unlawful.<sup>1</sup>

#### §4. EXCLUSIVE DEALER ARRANGEMENTS

Among the logical accompaniments of the changes in the commercial system and in commercial methods described in an earlier chapter should be noted an increase in the practice of making exclusive dealing stipulations in sales to distributors. This practice is very different from and must not be confused with the policy of providing for exclusive representation in specified localities or regions. An exclusive dealer arrangement, as the phrase is commonly used, denotes an agreement between a manufacturer and a merchant that the latter will refrain from handling competing lines of goods in consideration of his being supplied with the former's products. An arrangement for exclusive representation puts the shoe on the other foot, and the manufacturer, in consideration of his products being stocked by the merchant, engages to refrain from selling his products to competing dealers in a prescribed territory. Thus, under a policy of making exclusive dealer arrangements, a number of merchants in any particular district might be selling the given manufacturer's product, but none of them would be offering for sale the like product of any competitor of that manufacturer. Under a policy of arranging for exclusive representation in various market areas, on the other hand, only a single merchant would be selling the given manufacturer's product in any particular district; and this merchant might also, though this is not ordinarily the case, be distributing the like products of numerous other manufacturers. There is nothing to prevent

<sup>1</sup> Pending a judicial review of some proceeding involving this issue, it would seem that the prospect of such a modification of present administrative policy is not entirely fanciful.

a combination of both of these policies. The exclusive features may be made reciprocal obligations and, in fact, not uncommonly are so made.

It is apparent that the policy of making sales to distributors contingent upon the assumption of exclusive dealing obligations cannot, at least in respect to its effect upon the relations among distributive agencies, contravene the basic principles of the anti-trust laws. In so far as such a policy affects the competitive process, it does so by its influence upon the range of market opportunity of competing manufacturers. It erects no bars among merchants. It tends only to fence off the particular merchants as a group from other manufacturers. How far is this permissible on economic grounds? Is it illegitimate under all circumstances? May the prevention of any unduly restrictive effects safely be left to the corrective influence of the free play of competitive interests among distributors?

That the policy in question may be wholly fair and unrelated to any scheme to hinder competitors becomes evident upon consideration of the circumstances surrounding its widespread adoption latterly. Two characteristics of modern trade appear particularly to have fostered the adoption of the policy of requiring exclusive dealing. First, is the tremendous increase of mechanical devices of various kinds in proportion to all other products distributed. Mechanical and electrical equipment, ranging from sewing machines to the radio and from bicycles to airplanes, form an increasingly significant factor in the gross volume of trade. These goods tend to be relatively expensive and non-essential, requiring intensive sales effort for their distribution. They are also relatively intricate, requiring detailed explanation, demonstration, and even instruction in their uses. And they not infrequently require subsequent special services for their maintenance in operating order. Under these circumstances, the stipulation of exclusive dealing is practically indispensable for the vigorous and effective distribution of the goods. At best, the turnover of such products is bound to be relatively slow, and it is a vital interest of the manufacturer, therefore, to secure the full and whole-hearted cooperation of every distributor in the endeavor to attract the ultimate consumer.

This cannot be obtained, obviously, if the dealer is offering several competing lines of goods of substantially the same quality and price. It is in the dealer's own interest, also, to concentrate on the sale of a single manufacturer's line of such products. The dealer becomes in effect a partner of the producer interested in the successful distribution of the particular line of products, and will profit in proportion as his turnover on these goods increases under the stimulus of an undivided attention to their sale.

In the second place, the enormous growth in branded merchandise of all kinds has tended in a manner to choke the channels of distribution. So long as most goods were not differentiated by special trade-marks, but were differentiated simply by quality, size, and color according to common, simple standards, the distributor, particularly the jobber, could increase the number and range of his customers practically indefinitely without necessitating a disproportionate increase in stock. Additions to demand could be satisfied from additional drafts upon existing stocks or sources of supply. But with the multiplication of brands there has been imposed upon dealers in many lines of trade a choice between seeking wider custom and accumulating an ever wider range of substantially identical goods under competing brands, on the one hand, and, on the other hand, foregoing wider custom and concentrating intensively on the effective distribution of a single line of products for each class of goods handled. A choice of the former policy means the relegation of the jobber or dealer to the functions of a mere depot and delivery agency in the distributive process.<sup>1</sup> Not only have many distributors found such a position untenable from the business point of view, but manufacturers incline to withdraw from dependence upon any such slot-machine-like agency for the marketing of their goods. The alternative, which has been adopted more and more in recent years, is the stipulation of exclusive dealing upon all distributors with whom trade relations are maintained.

<sup>1</sup> Confusion must be avoided between the question of handling a wide range of non-competing goods—a necessity, for example, in the grocery trade—and the question of handling (whether in one department or in the business as a whole) a line of products from a single manufacturer or a number of similar lines of products from competing manufacturers. The latter is the sole question under discussion at this point.

The wisdom of the reservation provided in the Clayton Act should be clear from a consideration of these circumstances affecting the adoption of exclusive dealing arrangements. It will be recalled that Section 3 of that Act condemned an "agreement or understanding that . . . the purchaser (of goods) shall not . . . deal in the goods . . . of a competitor, or competitors of the . . . seller" *only when* "the effect of such . . . agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce." A device adopted for the purpose of securing greater efficiency in the distribution of a manufacturer's products must, under normal circumstances, tend to stimulate competition rather than to lessen it.<sup>1</sup> It does not follow, however, that because perfectly legitimate business considerations have led to the stipulation of exclusive dealing in many instances that such arrangements may not become oppressive and unfair under other circumstances. Unfairness exists in connection with this policy whenever the arrangements are intended to effect the exclusion of competitors from any market. And, in the law, this intention will be implied if the arrangement tends actually to achieve such exclusion, however innocent the real motive. It is obvious that exclusion of competitors from an opportunity to sell to a particular dealer does not necessarily exclude them from the given market, and is not in itself unfair. Such exclusion occurs whenever a manufacturer makes a sale. The question in every case is whether or not the necessary consequences of such obstruction of the ordinary channels of trade as the stipulation of exclusive dealing by the given manufacturer involves, bars the access of competing manufacturers to any section of the market or places their entrance under a handicap disproportioned to their relative efficiency and advantages of location.

The circumstances which may tend to give an obstructive and unfair character to exclusive dealing arrangements vary

<sup>1</sup> Indirectly, in practice, competitors may well be advantaged more by the disappearance of the given manufacturer's product from the stocks of a number of dealers than disadvantaged by the exclusion, in practical effect, of their own products from the stock of the given dealer. It is not necessarily a consequence, but, as already indicated, it very frequently occurs that an arrangement for exclusive dealing can be secured only by a reciprocal arrangement for exclusive representation.

from one trade to another. And usually it takes a combination of these circumstances to produce a restrictive effect rendering the practice properly subject to administrative correction. Perhaps the most obvious factor conditioning the legitimacy of the policy is the size of the producer adopting it. Size is a prerequisite to the unfairness of the practice, rather than an essential element in the unfairness, however. It is simply that a small producer, one among many, could in no event effectively cut off competitors from the markets for their goods. Such a manufacturer possesses insufficient leverage upon distributors to "tie up" enough of them to preempt the channels of distribution for his product. In the absence of a substantial control of production, therefore, it may be accounted an economic impossibility for a producer to work any injury to competitors by selling only to distributors engaging not to handle the competing products.

In the leading case interpreting the Clayton Act prohibition of exclusive dealing contracts, *Standard Fashion Co. v. Magrane Houston Co.*,<sup>1</sup> the Supreme Court rested its decision largely upon the fact that the petitioner, a manufacturer of dress patterns, was a dominating factor in its field. This case arose out of the violation by a Boston department store of its contract with the Standard Fashion Company. It was the contention of the defendant that this contract was void as being contrary to the Clayton Act since it provided that the department store should handle exclusively the patterns supplied by the plaintiff. In passing upon this issue the district court held that the contract was not one of agency but of sale and, noting that there was no provision for exclusive representation and that the plaintiff with two other allied companies controlled two-fifths of the 52,000 pattern agencies in the United States, reached the conclusion that it tended to substantially lessen competition.<sup>2</sup> This decision was affirmed by the circuit court of appeals<sup>3</sup> and subsequently by the United States Supreme Court.<sup>4</sup> The latter, referring again to the Fashion Company's control of distributing agencies, quoted with approval the circuit court's statement that, "The restriction of each merchant to one pattern manu-

<sup>1</sup> 258 U. S. 346 (1922).

<sup>2</sup> 259 Fed. 793 (1919).

<sup>3</sup> 254 Fed. 493 (1918).

<sup>4</sup> 258 U. S. 346 (1922).

facturer must in hundreds, perhaps in thousands, of small communities amount to giving such single pattern manufacturer a monopoly of the business in such community. Even in the larger cities, to limit to a single pattern maker the pattern business of dealers most resorted to by customers whose purchases tend to give fashions their vogue, may tend to facilitate further combinations; so that the plaintiff, or some other aggressive concern, instead of controlling two-fifths, will shortly have almost, if not quite, all the pattern business."<sup>1</sup>

Substantially identical contracts have been the basis of a proceeding instituted by the Federal Trade Commission against the Butterick Company, which controls the Standard Fashion Company and several other pattern making concerns.<sup>2</sup> The respective branches of the combine were found by the Commission to be using similar exclusive dealing contracts in selling their products to approximately 20,000 distributors of patterns in the United States.<sup>3</sup> On the basis of these facts the Commission ordered the respondents to cease and desist from selling patterns upon any contract or agreement that the distributor should not deal in the patterns of competitors.<sup>4</sup> In view of the close similarity of the facts in this proceeding with those in the earlier civil case, the validity of the Commission's ruling would not seem to have been questionable. Nevertheless, the Butterick Company appealed the case to the circuit court of appeals, where the decision fully sustained the order of the Commission.<sup>5</sup>

The significance of the factor of size also appears to be

<sup>1</sup> *Ibid.*, p. 427.

<sup>2</sup> The Standard Fashion Co. and the New Idea Pattern Co. were consolidated in 1920 as the Designer Publishing Company, Inc. One-half of the stock of the latter is owned by the Federal Publishing Company, which also owns all of the stock of the Butterick Publishing Company. The parent concern, the Butterick Company, owns the Federal Publishing Company and the other half of the stock in the Designer Publishing Company.

<sup>3</sup> The Butterick Publishing Co. had contracts with about 9,500 dealers, the Standard Fashion Co. with 6,000, and the New Idea Pattern Co. with 4,000.

<sup>4</sup> *Butterick Co., et al.*, 6 F. T. C. 310 (1923). The order also forbade use of contracts or agreements for maintaining resale prices. The respondent had during the course of the proceedings applied, without success, to the circuit court of appeals for an order restraining the Commission from proceeding with its trial of the case.

<sup>5</sup> *Butterick Co. v. Federal Trade Commission*, 4 Fed. (2d) 910 (1925). The Butterick Company, upon February 14, 1925, petitioned the Supreme Court for a review of this judgment.



recognized and even stressed by the Federal Trade Commission in a recent complaint against the Q. R. S. Music Company.<sup>1</sup> The finding was made that the respondent controlled over 50 per cent of the business in player rolls. Exclusive dealing arrangements had been made at various times with some 475 dealers in musical instruments and accessories in the United States, and it appeared that such dealers were in general the largest in the trade. Inasmuch as player rolls evidently cannot be economically marketed separately or except in conjunction with musical instruments, the exclusive dealing policy might well have a very restrictive influence in these circumstances. On the other hand, there was no finding regarding the existence of exclusive representation arrangements or regarding the proportion of the music trade affected by the arrangements in question with 475 dealers. The Q. R. S. Company has filed an appeal for a review of the Commission's order, so that the question of the relation of potential monopoly to the validity of exclusive dealing arrangements may receive judicial examination in the near future.

Another factor which would appear to be requisite in the conjuncture of circumstances which may render exclusive dealing arrangements unduly restrictive and unfair, is the nature of the prevailing market practice. When the type of goods in question is commonly marketed through separate specialized distributive agencies, there is but slight chance that the adoption of this policy by a manufacturer, no matter of what size, will restrict the market outlets of his competitors. The initial obstacles to mercantile enterprise in such lines are relatively slight, and in any case, as already pointed out, distributors in these lines tend to find it advantageous from their own point of view to confine their attention principally to a single manufacturer's products or the lines of a very few manufacturers representing different quality, or price ranges. The distribution of automobiles, of musical instruments, and of farm machinery illustrate the conditions here described. But when the type of goods under consideration is normally distributed in conjunction with a considerable variety of other commodities, as, for example,

<sup>1</sup> *Q. R. S. Music Co.*, 7 F. T. C. 412 (1924).

thread or sugar, and cannot economically be marketed separately, the effect of a large manufacturer's adoption of exclusive dealer arrangements as a general policy tends to become rigidly obstructive.<sup>1</sup> Competing producers are not in a position to create new distributive agencies, and the principal distributors, because of the risk from alienating the largest and most dependable source of supply, may not be in a position to resist the demand for an exclusive dealing arrangement.

Illustrative of this situation are two cases in which orders to cease and desist have been issued by the Commission.<sup>2</sup> In both proceedings it appeared the products of respondents were specialties marketed by dealers in conjunction with a great variety of related devices obtained from numerous sources. In one instance the principal product was "rotary snap switches" sold chiefly by electric appliance shops, and in the other instance the principal products were horse-clipping and sheep-shearing machines sold chiefly through hardware jobbers. The respondent manufacturer of shearing machines had offered special rebates to dealers on the condition, among others, that they had not over a specified period bought or sold such machines made by any competing manufacturer.<sup>3</sup> In such circumstances, restrictions on the established agencies of distribution tend to become peculiarly oppressive upon competing manufacturers without yielding corresponding advantages, from the economic point of view, to the particular manufacturer stipulating the restrictions.

<sup>1</sup> It should be noted that changes sometimes occur in the method of distributing particular commodities, necessitating a re-examination of the effects of exclusive dealing arrangements. For example, tobacco products, at one time handled largely by wholesale grocers and druggists, are now sold to a considerable extent through special jobbers or directly to shops dealing almost exclusively in tobacco products and equipment.

<sup>2</sup> *Chicago Flexible Shaft Co.*, 1 F. T. C. 181 (1918); *Standard Electric Manufacturing Co.*, 5 F. T. C. 376 (1923).

<sup>3</sup> In the electric switch case, the findings of fact reveal that the exclusive dealing arrangements were made in consideration of exclusive representation in certain territory in each instance. The significance of this factor is discussed in the following paragraphs in the text. The importance of this consideration seems to have been lost to the Commission, however. After calling attention to the fact that the dealers bound by the exclusive dealing arrangements were also respondent's exclusive representatives, and declaring that "said dealers are engaged in competition in their respective territories with the distributors of manufacturers competing with the respondent," the order proceeded, notwithstanding, to forbid respondent to make sales "subject to the condition . . . that the purchaser . . . shall not deal in the goods . . . of any competitor of the respondent."

Finally, the interference resulting from exclusive dealing arrangements tends to become unfair and oppressive when it is unaccompanied by reciprocal arrangements for exclusive representation. If, instead, the policy is pursued of making special discounts, or like inducements, to every dealer who will agree not to handle competing lines, the purpose to hinder and harass competitors, regardless of the immediate consequences to one's own business, becomes manifest. This, as previously mentioned, was the situation revealed in the proceedings against the Chicago Flexible Shaft Company and clearly justified, when taken in conjunction with other circumstances there disclosed, the order to cease and desist. On the other hand, the Commission's failure to recognize the significance of this factor and the very decided difference which the presence of exclusive representation arrangements makes has led to its reversal by the courts in one instance.<sup>1</sup> In a complaint against the Pearsall Butter Company, the Commission charged the respondent with attempting to monopolize the manufacture and sale of margarin by refusing to sell its product to wholesale distributors except upon condition of exclusive dealing. According to the Commission's own findings, "at least twenty competitors of respondents have used contracts containing the exclusive dealing feature . . . in the same territory covered by respondent," while some sixty-five other competitors were also doing business in the same territory.<sup>2</sup> Nevertheless, an order to cease and desist was issued. Additional significant facts brought out in the judicial review of this case, not mentioned by the Commission, were: (1) that respondent was a minor factor in the trade, doing about one per cent of the total business, (2) that no effort was made to impose exclusive dealing arrangements on retail dealers, and (3) that the consideration of the exclusive dealing feature was an exclusive representation arrangement. Under these circumstances, the impolicy of the Commission's order should be obvious. As the court declared, "The record in this case discloses no facts or circumstances which would justify the

<sup>1</sup> *B. S. Pearsall Butter Co.*, 5 F. T. C. 127 (1922); *B. S. Pearsall Butter Co. v. Federal Trade Commission*, 292 Fed. 720 (1923).

<sup>2</sup> 5 F. T. C. 129 (1922).

conclusion that there was shown more than the 'mere possibility of the consequences described.'<sup>1</sup> The commercial policy of stipulating for exclusive dealing on the basis presented in this case is clearly fair and within the Clayton Act reservations referred to above.

So far this discussion has been confined to exclusive contracts between producers and jobbers or merchants. A similar method may also be employed as between the producers and consumers of materials used in the production of other commodities.<sup>2</sup> Provided such exclusive agreements are not designed primarily to crush small competitors and are not used in connection with a discriminatory policy,<sup>3</sup> there seems to be no ground for regarding them as unfair or in any way a departure from normal competitive methods. There is, in such case, no preemption of the channels of distribution. The exclusive feature of the sales contract under these conditions is ordinarily a necessary protection to the seller, who offers the goods at a special rate fixed in anticipation of a certain volume of purchases, contingent only upon the scale of operations of the buyer. Competitors are given the alternative of offering their goods on better or equivalent terms or of losing the business. This situation typifies the whole competitive process and tends in no way to "lessen competition."<sup>4</sup>

Another business arrangement outwardly similar to exclusive dealing agreements, but in substance vitally different, is the restriction upon the activities of agents by their principals. It need hardly be insisted that where the genuine agency relation exists there can be nothing unfair or oppressive in the stipulation by a principal that his agent shall not buy

<sup>1</sup> 292 Fed., 722 (1923).

<sup>2</sup> For example, in the sale of sugar and glucose to manufacturing confectioners.

<sup>3</sup> If the attempt were made to secure exclusive contracts from the customers of a particular competitor by offering special price concessions, such a policy, persistently pursued, might be regarded as unfair. Its unfairness would consist primarily, however, in its resemblance to local price-cutting, i. e., in its discriminative features.

<sup>4</sup> The Commission has issued one order in a case of this kind, *Galena Signal Oil Co.*, 2 F. T. C. 446 (1920). The respondent in this case guaranteed its railroad customers that the cost of lubrication should not exceed a certain amount per 1,000 car miles, provided respondent's lubricants were used exclusively. Notwithstanding the apparent reasonableness of this arrangement, the Commission forbade the respondent to continue making such contracts, *ibid.*, p. 459. The order was not contested in the courts.

or sell competing goods. So far, indeed, from such a stipulation being unfair, it would in law be ground for the breaking of the agency contract were an agent to engage in such an activity without the consent of the principal, even in the absence of any express restriction of that nature in the contract.<sup>1</sup> It is true that in practice it is often difficult to distinguish between an agent and an independent dealer or contractor, owing to the complexity of actual business affairs. Only on the ground of a mistaken interpretation of facts does it seem possible to account for the action of the Federal Trade Commission in ordering the Curtis Publishing Company to cease and desist from requiring the wholesale distributors of its magazines not to handle competing publications.<sup>2</sup> In upholding the Circuit Court of Appeals' reversal of the order, the Supreme Court, after reviewing the facts, declared: "Judged by its terms, we think this contract (between respondent and its distributors) is one of agency, not of sale upon condition, and the record reveals no surrounding circumstances sufficient to give it a different character. This, of course, disposes of the charges under the Clayton Act. The engagement of competent agents obligated to devote their time and attention to developing the principal's business, to the exclusion of all others, where nothing else appears, has long been recognized as proper and unobjectionable practice."<sup>3</sup>

In conclusion, it may be observed that the regulation of this business practice by the Federal Trade Commission indicates a lack of any systematic analysis of the issues it presents. Apparently there has been no settled policy and no reasoned conviction upon the nature and scope of the Commission's jurisdiction in this class of cases. Altogether some

<sup>1</sup> See, for example, *Seaburn v. Zachmann*, 99 N. Y. App. Div. 218 (1904).

<sup>2</sup> *Curtis Publishing Co.*, 2 F. T. C. 20 (1919). The exclusive features of the Curtis Publishing Company's distributive system had previously been unsuccessfully attacked in a civil action under Section 16 of the Clayton Act. See: *Pictorial Review Co. v. Curtis Publishing Co.*, 255 Fed. 206 (1917).

In a recent article Mr. Gregory Hankin expresses the view that there was ample evidence to support the findings of the Commission in this case; but it is submitted the courts were correct in regarding the issue of whether the system found by the Commission to exist constituted an agency arrangement or not as a question of law and not of fact. See: Gregory Hankin, "Conclusiveness of Federal Trade Commission's Findings as to Facts," 23 *Michigan Law Review*, 233, 262-267 (1925).

<sup>3</sup> *Federal Trade Commission v. Curtis Publishing Co.*, 260 U. S. 568, 574 (1923).

forty-five complaints have been issued, but only six orders to cease and desist have resulted from these proceedings, the others, save two at present pending, being ultimately dismissed. No class of cases better illustrates the lack of clarity in the Commission's rulings, moreover, under the present procedure. The cases dismissed, with few exceptions, fail to indicate, even approximately, the grounds upon which the Commission based its action.<sup>1</sup> And the orders do not, of course, disclose the essential relation which the Commission must have supposed to exist between the various situations complained of. A brief but explicit statement in connection with the numerous cases dismissed would have assisted greatly in an understanding of what factors or circumstances the Commission regards as determinative of unlawfulness.<sup>2</sup>

### §5. TYING CONTRACTS

With the growing use of mechanical devices in many aspects of modern life there has developed a close interrelationship between the consumption or use of various articles. This relationship may approach a functional interdependence, in some instances, between a mechanism and a certain type of raw material or between a mechanism and certain auxiliary equipment. The same interdependence is sometimes found between complementary ingredients in products, of which industrial chemistry in recent years has provided numerous examples, compounded of a variety of elements.

<sup>1</sup> The chief exceptions are Complaints No. 551-555 and 559-560, against various butter and butter substitute manufacturers, dismissed as a result of the adverse decision in *B. S. Pearsall Butter Co. v. Federal Trade Commission*, 292 Fed. 720 (1923). See Annual Report, 1924, p. 190.

In the case of the *Fruit Growers' Express*, 2 F. T. C. 369 (1920), in which the Commission's order was reversed, 274 Fed. 205 (1921), because of its want of jurisdiction over interstate carriers, we do, of course, have the explanation, but not from the Commission.

<sup>2</sup> Perhaps the best illustration of the shortcoming described is afforded by a number of complaints issued against various manufacturers of adding machines and typewriters. (Complaints 355-371, Annual Report, 1920, pp. 125-126.) The respondents were charged with giving rebates or discounts "with the object of causing . . . purchasers to confine their purchases to respondent's products." Unless unusual circumstances accompanied this policy, which there is no ground for assuming, the character of the commodity involved in these cases might, for reasons already developed in the text, well justify the employment of the policy of encouraging exclusive dealing. The Commission, however, makes no reference to this fact, the record merely stating that the cases were dismissed because the evidence was insufficient to support an order. Annual Report, 1922, p. 142.

The tying contract is a business practice which has developed to take advantage of these technical relationships. A manufacturer having obtained a certain degree of control over the production of one article or machine is in a position to require purchasers or lessees to take or secure from him also the necessary auxiliary or complementary articles. The close technical inter-relationship between the two articles or machines may justify the imposition of such a restriction or condition upon sales, or it may be used merely as a cover for extending the business and profits of the seller occupying a privileged position in the market in respect to one of the given articles. No general rule can be laid down, therefore, regarding the fairness or legitimacy of the use of tying contracts. It depends upon the particular circumstances of each case. And in any event, it should be evident, there is nothing fraudulent or unethical in the practice.

The simple question which tying contracts present is of the limits to which an acquired economic power in one field or with respect to one article of commerce may be used as a leverage for developing new business in another direction. For it is plain that the sale or lease of one article solely upon condition that a stipulated quantity or number of another article or articles be bought or leased from the same concern imposes a handicap, other things being equal, upon the first article. And this handicap or burden must in a competitive market tend to be reflected in a diminished demand for that article. Under freely competitive conditions, therefore, the adoption of the policy of the tying contract would tend to hinder the distribution of one product as much as it fostered the distribution of the other or "tied" product. There could be no advantage in the employment of such a policy not offset by a commensurate disadvantage. Commercially speaking, when the products the sale or lease of which are "tied" together are both subject to free competition, the tying policy would not normally be profitable. But there are various circumstances which may place one product of a given concern beyond the reach or at least beyond the effective interference of competition. A patent, control of a particular raw material, a secret process, a strong consumer goodwill—these are not uncommon shields protecting a given prod-

uct from the brunt of competitive attack. Demand may be diverted, of course, from even the most rigidly protected article, e. g., one that is patented, if the handicaps imposed upon its distribution are severe. But within reasonable limits a concern may find it profitable to exploit its favored position in the marketing of such a product by attaching to its sale or lease the condition that other products be purchased or leased with it.

It should be noted that the federal regulative measures of 1914 did not specifically prohibit tying contracts in the ordinary form, let alone under all circumstances. The third section of the Clayton Act forbade sales or leases upon the condition that products of competitors should not be used or dealt in by the purchaser or lessee only when the effect might be substantially to lessen competition or to create a monopoly. This prohibition obviously does not touch the more common form of the tying contract in which the condition is only that other products of the seller or lessor must be purchased or leased in conjunction with a specific product. Such a restriction and the one prohibited by the Clayton Act might have a like effect, of course, but not necessarily. They would tend to produce identical results only in case of a technological or consumptive interdependence between the products "tied" together. But the broad prohibition of unfair methods of competition in the Federal Trade Commission Act appears to cover the use of tying contracts in the second form above mentioned, when such a policy does actually have a restrictive effect upon competitors.

One of the early orders of the Federal Trade Commission condemning this practice treated it as a violation of Section 5 of the Trade Commission Act, and the unfairness seems to have been regarded as residing in the essential nature of the tying contract policy.<sup>1</sup> In reviewing this order the Supreme Court made it clear, however, as should have been clear without its pronouncement, that tying contracts are not under all circumstances unfair or illegitimate.<sup>2</sup> It appeared that the respondents in this proceeding, who were distributors of cotton compress supplies, had adopted the general policy of

<sup>1</sup> *Warren, Jones & Gratz*, 1 F. T. C. 249 (1918).

<sup>2</sup> *Federal Trade Commission v. Warren, Jones & Gratz*, 253 U. S. 421 (1920).



refusing to sell the steel ties used for binding bales of cotton unless the purchaser also purchased a certain quantity of jute bagging.<sup>1</sup> As the quantity of bagging required for the bales of cotton bound with a given number of ties could be closely estimated, the requirement was so adjusted that the respondent's bagging was used to the exclusion of bagging from any other source upon the bales bound with ties furnished by it. This was equivalent in effect, therefore, though not similar in form, to the tying contracts prohibited under specified circumstances in the Clayton Act. The order to cease and desist, however, was based solely on the fifth section of the Trade Commission Act. In setting aside this order, the Supreme Court pointed out that the scope of the Commission's orders must, upon general principles of law, be limited to the charges made in the complaint, and as the complaint in this case made no allegations respecting the monopolistic position or intention of the respondents in respect to either of the articles in question, the order could not be rested on facts of this nature appearing initially and solely in the findings as to the facts. On this technical ground there was excluded all evidence of the dominant control of the steel cotton-tie market by the respondents as exclusive agents of the Carnegie Steel Company, which it appeared manufactured approximately three-fourths of all such ties produced in the United States. With evidence of this vital character excluded, nothing unfair was found in the policy attacked. "The complaint contains no intimation," said the court, "that Warren, Jones & Gratz did not properly obtain their ties and bagging as merchants usually do; the amount controlled by them is not stated; nor is it alleged that they held a monopoly of either ties or bagging or had ability, purpose or intent to acquire one. . . . All question of monopoly or combination being out of the way, a private merchant, acting in entire good faith, may properly refuse to sell, except in conjunction, such closely associated articles as ties and bagging."<sup>2</sup> On the issue as thus framed certainly the decision was unexceptionable.

<sup>1</sup> 1 F. T. C. 255. This finding was questioned, however, by the Circuit Court of Appeals, 258 Fed. 314, 318.

<sup>2</sup> 253 U. S. 428.

This interpretation of the limited scope of the Federal Trade Commission's authority in regulating the use of tying contracts has subsequently been confirmed by the extension of a like limitation to proceedings under the third section of the Clayton Act, where the form of the tying arrangement makes that section applicable. In a considerable group of cases, involving the lease of oil tanks and pumps, the Commission held it was unlawful as tending to the creation of monopoly for petroleum refiners to lease such equipment to dealers on condition that the lessee should use it exclusively for oil or gasoline purchased from the lessor.<sup>1</sup> In reaching this conclusion two important circumstances appear to have been ignored, either one of which might have been sufficient to take the contracts in question out of the class of illegal business practices. The two together, however, plainly indicate the legitimacy of the practice complained of. In the first place there was no monopolistic control, as the findings themselves disclosed, of either the tanks and pumps or of the oil and gasoline. The several competing refiners were able and did provide such pumps for their respective dealers, for the most part on similar but not identical terms. Dealers having sufficient capital were in no way hindered from buying the equipment outright. And such dealers apparently found no difficulty in procuring their supplies of oil and gas from any of the refining companies upon non-discriminatory terms. In the second place, none of these leases, so far as the evidence showed, bound any dealer to purchase oil or gasoline exclusively from the lessor. The requirement was only that the particular equipment leased should not be used in connection

<sup>1</sup> Altogether forty-one cases of this character were brought, and twenty-seven orders to cease and desist were issued. *Sinclair Refining Co.*, 2 F. T. C. 127 (1919); *Standard Oil Co. of Ind.*, 2 F. T. C. 26 (1920); *same*, 2 F. T. C. 46 (1920); *Maloney Oil Mfg. Co.*, 2 F. T. C. 346 (1920), and list of cases following; *Lubric Oil Co.*, 3 F. T. C. 68 (1920); *Bartels Oil Co.*, 3 F. T. C. 77 (1920); and *Motor Fuel & Lubricating Co.*, 3 F. T. C. 78 (1920), and list of cases following. There is some confusion in the record of these cases, due to duplication and the modification of orders. Cf. G. C. Henderson, "The Federal Trade Commission," *op. cit.*, p. 309.

In five of the cases cited the original complaints do not appear to have included a charge against the leasing of equipment on restrictive terms. Compare, for example, the summary of Complaint No. 85, against the Standard Oil Co. of Indiana, Annual Report 1918, p. 64, with the case as reported, 2 F. T. C. 26 (1920), also Complaint No. 133, against the same company, Annual Report 1918, p. 70, with case as reported, 2 F. T. C. 46 (1920). The two orders to cease and desist appear to be identical, although addressed to the same respondent.

with the sale of any oil or gasoline other than that furnished by the lessor. Each dealer was privileged to lease tanks and pumps of as many different refiners as he desired. The channels of distribution were still open to competitors generally. In view of these circumstances, it is not strange that many of the orders in question were appealed to the courts. In several instances the court found that no interstate commerce was involved and accordingly dismissed the orders.<sup>1</sup> In some of the other cases the circuit courts of appeals held that the evidence did not establish the violations of the Trade Commission Act and the Clayton Act charged.<sup>2</sup>

The Supreme Court, upon appeal, in a consolidated action affirmed these rulings.<sup>3</sup> After calling attention to the circumstances above recited, the Court declared, "The contract, open and fair upon its face, provides an unconstrained recipient with free receptacle and pump for storing, dispensing, advertising and protecting the lessor's brand. The stuff is highly inflammable and the method of handling it is important to the refiner. He is also vitally interested in putting his brand within easy reach of consumers with ample assurance of its genuineness. No purpose or power to acquire unlawful monopoly has been disclosed, and the record does not show that the probable effect of the practice will be unduly to lessen competition. Upon the contrary it appears to have promoted the public convenience by inducing many small dealers to enter the business and put gasoline on sale at the cross-roads."<sup>4</sup>

Nowhere is there a better illustration, perhaps, of the failure of the Federal Trade Commission to realize in practice the abundant claims made by its promoters and adherents of the superiority of administrative procedure over the judicial process in dealing with business misfeasance. The contrast of the rigid rationalistic, purely technical inter-

<sup>1</sup> *Standard Oil Co. of N. Y. v. Federal Trade Commission*; *Texas Co. v. same*, 273 Fed. 478 (1921); *Canfield Oil Co. v. Federal Trade Commission* (and five other cases), 274 Fed. 571 (1921).

<sup>2</sup> *Sinclair Refining Co. v. Federal Trade Commission*, 276 Fed. 686 (1921); *Standard Oil Co. of N. J. v. Federal Trade Commission* (and two other cases), 282 Fed. 81 (1922).

<sup>3</sup> *Federal Trade Commission v. Sinclair Refining Co., et al.*, 261 U. S. 463 (1923).

<sup>4</sup> *Ibid.*, p. 475.

pretation of its regulative powers in these oil pump cases by the Commission, and its apparent indifference to the concrete, meliorative circumstances surrounding the alleged unfair practice, with the realistic, flexible, and sensible treatment of the issues presented by the courts is worthy of serious reflection. The unmerited depreciation of judicial procedure, on the one hand, and the uncritical praise of all that passes for adequate substitute, on the other hand, receive a convincing answer in the record of these proceedings.

After its decisive defeat in the oil pump cases, the Commission appears to have realized that the categorical policy it had been pursuing in the regulation of tying contracts was insupportable. Orders of dismissal rescinding earlier orders to cease and desist were entered in three cases involving the practice of coffee merchants in leasing or loaning coffee urns to customers conducting restaurants, hotels and like establishments on condition that the coffee used should be purchased exclusively from the lessor.<sup>1</sup> It is difficult to understand how this arrangement could have been regarded as prejudicial to competing coffee roasters. The customers in question were not dealers, and there could, therefore, be no question of obstruction of the channels of trade, in the usual sense of that term. The arrangement was terminable by either party, in one case upon five days' notice<sup>2</sup> and in the other cases apparently at will, so that the customer was bound to buy exclusively from the given merchant only so long as he was satisfied with the product and the terms upon which it was supplied. In the absence of any evidence of the possession of a monopolistic position or intention by the respondent coffee roasters either with respect to the equipment which they, like the refiners in the oil pump cases, purchased from independent manufacturers, or with respect to the coffee, there would seem to be no adequate ground for considering the tying contracts in question unfair methods of competition.<sup>3</sup>

<sup>1</sup> *Kronberger & Co.*, 2 F. T. C. 399 (1920); *John H. Wilkins Co., Inc.*, 2 F. T. C. 403 (1920); *The Levering Coffee Co.*, 2 F. T. C. 407 (1920). The orders of dismissal were entered on November 13, 1923. See Annual Report, 1924, p. 190, and 7 F. T. C. 28.

<sup>2</sup> The *Levering* case, *op. cit.*, p. 409.

<sup>3</sup> No violation of Section 3 of the Clayton Act was alleged.

If tying contracts do not always hamper competition, however, under some circumstances such arrangements may have that effect. And in certain proceedings the Commission has been more fortunate in choosing the ground for its attack than in those reviewed up to this point. In three early cases the respondents were found to have attempted to utilize patent rights for the extension of control over unpatented articles.<sup>1</sup> The use of even a legitimate monopolistic privilege of this character for fostering the sale of non-monopolized articles commonly used or sold in conjunction therewith gives a market advantage to the patentee in respect to the sale of the unpatented goods wholly unrelated to his economic position relative to the production and distribution of such goods. There is a corresponding restriction of the market for competitors producing or dealing in the unpatented articles which bears no essential relation to their comparative industrial efficiency or trade good-will. Tying contracts under these circumstances are clearly within the jurisdiction of the Federal Trade Commission, for it was in part as a consequence of the reaction to a decision based upon a contrary view that the prohibition contained in Section 3 was incorporated in the Clayton Act.<sup>2</sup>

While it seems to be settled law now that the scope of the legislative prohibition extends to every tying contract in which a seller possesses a monopolistic control over one of the articles sold or leased only in conjunction,<sup>3</sup> it seems worthy of consideration that there are circumstances which from the economic point of view might furnish some justification for tying contracts even when based upon such exclusive privileges as a patent affords. This was illustrated in the United Shoe Machinery case. The defendant there had pursued the general policy of leasing the machines manufactured by it, instead of selling them outright to shoe manufacturers. That this leasing system, as such, was beneficial to the trade

<sup>1</sup> *A. B. Dick Co.* 1 F. T. C. 20 (1917); *National Binding Machine Co.*, 1 F. T. C. 44 (1917); *Chamberlain Cartridge & Target Co.*, 2 F. T. C. 357 (1920).

<sup>2</sup> *Henry v. A. B. Dick Co.*, 224 U. S. 1 (1912). See Chapter III, *infra*, p. 9. Consult, also, National Industrial Conference Board, "Trade Associations: Their Economic Significance and Legal Status," New York, 1925, p. 133.

<sup>3</sup> *Motion Picture Patents Co. v. Universal Film Manufacturing Co.*, 243 U. S. 502 (1917); *U. S. v. United Shoe Machinery Co.*, 258 U. S. 451 (1922).

and not subversive of competition was expressly recognized by the Supreme Court in a previous unsuccessful prosecution under the Sherman Act.<sup>1</sup> If this be granted, several of the restrictive clauses in the leases which the Government attacked take on a far from vicious aspect. For example, the so-called "restricted use" clause provided that the leased machinery should be used only in the manufacture of shoes on which other specified operations had been performed by machinery obtained from the United Company. Since the practice was for the lessor to keep these machines in repair, and since the amount of the royalty in any period depended upon the constancy of operation, there is some weight in the contention of the defendant that, as the machines were designed for use together and when so used were less subject to breakdown, this clause afforded only reasonable protection to the lessor. It was also contended that this clause was necessary in some instances in order to assure an accurate accounting for the work done upon certain auxiliary machines to which it was not feasible to attach recording mechanisms.

Notwithstanding these considerations, the Supreme Court held that the restrictive features of the leasing system revealed in this case contravened the express provisions of the Clayton Act. In determining that the operation of the leases in question did tend to produce the effect of substantially lessening competition or of creating a monopoly, it is difficult to escape the conclusion that the Court was influenced by the formidable size of the defendant in this particular action. It pointed out that the United Company controlled more than 95 per cent of the shoe machinery business in the United States.<sup>2</sup> "When it is considered," said the Court, "that the United Company occupies a dominating position in supplying shoe machinery of the classes involved, these covenants signed by the lessee and binding upon him effectually prevent him from acquiring the machinery of a competitor of the

<sup>1</sup> *U. S. v. United Shoe Machinery Co.*, 247 U. S. 32 (1917). The court said, p. 62, "The testimony also shows that the advantage of the leases was and is that manufacturers of not large means were able to obtain machinery which they were without capital to buy. They helped, indeed, the big and the little. . . . We must assume that they were entered into by the lessees upon a calculation of their value—the efficiency of the machines balanced against the restrictions upon and conditions of their use."

<sup>2</sup> 258 U. S., 455.

lessor except at the risk of forfeiting the right to use the machines furnished by the United Company which may be absolutely essential to the prosecution and success of his business."<sup>1</sup> Nevertheless, in sweeping terms, the Court condemned tying contracts of every type, under the circumstances presented; "We can entertain no doubt," the Court declared, "that such provisions as were enjoined are embraced in the broad terms of the Clayton Act which cover all conditions, agreements or understandings of this nature."<sup>2</sup> In view of this unequivocal declaration, it appears that as long as the Clayton Act remains in force in its present form it will be unlawful for a patentee or for any other holder of a substantial monopoly in respect to one product to make its sale or lease contingent upon an agreement of the purchaser or lessee not to use with it or upon it other devices or materials not produced by the seller or lessor.

#### §6. CONSPIRACIES IN RESTRAINT OF TRADE

That it is possible through certain forms of collective or group action to interfere with the free course of trade to the injury of outside interests, even without resort to means in themselves illegal, has long been recognized in the law.<sup>3</sup> It is the basis of the doctrine of conspiracy, reaching back into the early stages of common law development. There is a coercion in numbers, as some judicial authority has said, which exceeds the casual pressure from the uncoordinated, individual action of the several members of the group. Whether this concerted action is fair or unfair, legal or illegal, depends upon the ends to which the combined forces are exerted and the methods of their exertion. There is nothing

<sup>1</sup> *Ibid.*, p. 458.

<sup>2</sup> *Ibid.*, p. 457.

<sup>3</sup> Perhaps the most common and best understood application of this principle is in labor boycott cases, but the principle itself is general and fundamental. This is indicated by the broad terms of a recent important decision of the Supreme Court in which it was declared: "The substance of the matters here complained of is an interference with complainant's interstate trade, intended to have coercive effect upon complainant, and produced by what is commonly known as a 'secondary boycott.' . . . It is settled . . . that such a restraint produced by peaceable persuasion is as much within the prohibition as one accomplished by force or threats of force; and it is not to be justified by the fact that the participants in the combination or conspiracy may have some object beneficial to themselves or their associates." *Duplex Printing Co. v. Deering*, 254 U. S. 443, 466-468 (1921).

unethical in joint endeavor, as such. But when directed to the injury of a competitor or the compulsion of a business concern to do that which it otherwise would, in its own interest, refrain from doing, it comes fully within the settled principles of restraint of trade. Concerted action for such objects becomes as pernicious from the economic point of view and as illicit from the legal point of view as any conspiracy to raise prices, curtail production, or divide market territory.<sup>1</sup>

Since neither the common law nor the Sherman Act made any distinction between conspiracies to interfere with, obstruct, or coerce producers or traders in their business operations and conspiracies to mulct the general public, but condemned both alike, it might appear that this whole subject required no further regulation, and that it would require a specific delegation of power to bring it within the jurisdiction of the Federal Trade Commission. So far from this being the case, however, the Commission has assumed the authority to deal not only with conspiracies to thwart particular business rivals and interfere with the operations of outsiders,<sup>2</sup> which might be inferred to lie within its jurisdiction under an elastic construction of the phrase "unfair methods of competition," but also with conspiracies simply to stifle competition among the conspirators.<sup>3</sup> It should be manifest that upon neither a technical, nor a popular, nor a literal interpretation of Section 5 of the Trade Commission Act, from which alone can the Commission draw any power to act in such cases, is there any warrant for a proceeding under that section against a combination of traders to fix prices, for example. The offense, if offense there be, in such a case is not in the way in which the several traders compete, their "methods of competition," but in the fact of their failure or refusal to compete at all. If there is a violation of law it is a violation of the Sherman Act and is properly sub-

<sup>1</sup> See for a full discussion of this subject: National Industrial Conference Board, "Trade Associations: Their Economic Significance and Legal Status," New York, 1925, Part II, pp. 61-93.

<sup>2</sup> For example, *Botiford Lumber Co., et al.*, 1 F. T. C. 60 (1918). Other cases of this nature will be listed below.

<sup>3</sup> For example, *Association of Flag Manufacturers*, 1 F. T. C. 55 (1918). Other cases will be cited below.



ject to the penal procedure therein provided. No indication has ever been given by the Commission that it regards its assumed power in this class of cases as extending beyond the reach of the Sherman Act in any respect. Such being the situation, it may well be doubted that it conforms to the public interest to attempt to apply an essentially remedial statute, wholly lacking in punitive provisions, to a type of business arrangement which is subject to prosecution under a penal statute. And, as already suggested,<sup>1</sup> as a mere matter of administrative efficiency there is every reason for concentrating the responsibility for the enforcement of the Sherman Act in one governmental department, the Department of Justice, especially since the Sherman Act is a criminal statute.

Nevertheless the Federal Trade Commission, in line with the policy indicated, has devoted not a little attention to concerted arrangements for various purposes among trade competitors, and thus far it has been upheld by the circuit courts of appeals in every instance in which its orders dealing with activities of this kind have been challenged.<sup>2</sup> The attitude of the Supreme Court towards action by the Commission in cases of this character has not been revealed, however. The proceedings of the Commission fall into three main groups. There are, first, several cases in which the orders were directed primarily if not solely, against price

<sup>1</sup> See *supra*, Chapter IV, Section 4. It may be pointed out also, that on the ground of expedition there would seem to be no advantage in the administrative procedure over the ordinary judicial procedure. While in some of the earlier cases decisions were obtained with considerable celerity, e. g., *Association of Flag Manufacturers*, Complaint filed September 14, 1917, decided January 29, 1918; *U. S. Gold Leaf Manufacturers Assn.*, Complaint filed April 15, 1918, decided June 28, 1918. These instances are offset by others in which complaints filed in 1918 were still pending on June 30, 1924. *Photo-Engravers' Club of Chicago*, Complaint No. 82, consolidated with Docket 928, Annual Report, 1924, p. 195; *National Wholesale Druggists' Assn.*, Complaint No. 168, Annual Report, 1924, p. 195. The latter case was dismissed, September, 1924.

<sup>2</sup> All but one of the five cases of this nature which have been reviewed by the courts dealt with conspiracies to coerce outsiders to assist in maintaining "legitimate" channels of trade: *National Harness Manufacturers Assn. v. Federal Trade Commission*, 268 Fed. 705 (1920); *Western Sugar Refining Co. v. Federal Trade Commission*, 275 Fed. 725 (1921); *Wholesale Grocers of El Paso v. Federal Trade Commission*, 277 Fed. 657 (1922).

The other case, besides involving the issue of conspiracy to coerce, dealt with price-fixing arrangements. *Pacific Coast Paper Trade Assn. v. Federal Trade Commission*, 4 Fed. (2d) 457 (1925).

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manipulation.<sup>1</sup> Secondly, there are a number of cases in which associations of distributors were found to have cooperated to enforce the use of regular or "legitimate" channels of trade.<sup>2</sup> Finally, the Commission has condemned in a few cases collective action for the attainment of diverse objects such as a guarantee against price decline, special discounts, and the open shop.<sup>3</sup> Into whichever one of these groups a proceeding may fall, the essential question in every instance is whether or not restraint of trade resulted from the facts disclosed. The examination of the necessary elements in a restraint of trade and the factors bearing upon its illegality would be out of place here. It would amount to testing the jurisdiction of the Federal Trade Commission by discussing the question of what constitutes a violation of the Sherman Act. That inquiry has already been made in an-

<sup>1</sup> *Bureau of Statistics of Book Paper Manufacturers*, 1 F. T. C. 38 (1917); *Association of Flag Manufacturers*, 1 F. T. C. 55 (1918); *U. S. Gold Leaf Manufacturers' Assn.*, 1 F. T. C. 173 (1918); *Blakely Printing Co., et al.*, 1 F. T. C. 277 (1918); *Music Publishers' Assn.*, 5 F. T. C. 465 (1923); *United Typothetae*, 6 F. T. C. 445 (1923); *Standard Oil Co. of Ky., et al.*, Complaint No. 1038, Order issued August, 1924.

<sup>2</sup> *Botsford Lumber Co., et al.*, 1 F. T. C. 60 (1918); *Wholesale Saddlery Assn.*, 1 F. T. C. 335 (1919); *Baltimore Hub-Wheel & Mfg. Co., et al.*, 1 F. T. C. 395 (1919); *Western Sugar Refinery, et al.*, 2 F. T. C. 151 (1919); *McKnight-Keaton Grocery Co., et al.*, 3 F. T. C. 87 (1920); *Wholesale Grocers of El Paso*, 3 F. T. C. 109 (1920); *Atlanta Wholesale Grocers*, 4 F. T. C. 466 (1922); *Southern Hardware Jobbers' Assn.*, 4 F. T. C. 428 (1922).

These cases all involved, at the minimum, the ordinary "secondary boycott," such as was under consideration in the Duplex Printing case referred to in a note at the beginning of this section, the difference being only that in these instances the conspirators were merchants instead of employees, and in some instances the means used were less harsh. In the Botsford Lumber case not only were manufacturers coerced to refrain from selling to certain competitors of the respondents, but numerous other harassing tactics were found to have been used against such competitors.

It may be observed that in the findings of fact in the Baltimore Hub-Wheel Company case the Commission failed to bring out any evidence of collusion between the two respondents in the proceeding. It appeared only that each of them, being automobile accessory jobbers, had threatened to withdraw its trade from a manufacturer unless he ceased allowing the same discount to certain retailers as was allowed to jobbers. In the absence of some agreement or understanding between the respondents there would seem to be nothing unlawful in this conduct. See *Federal Trade Commission v. Raymond Bros.-Clark Co.*, 263 U. S. 553 (1924).

<sup>3</sup> *Cigar Manufacturers' Assn. of Tampa, Fla.*, 5 F. T. C. 1 (1922); *St. Louis Wholesale Grocers' Assn.*, 7 F. T. C. 1 (1923); *Wisconsin Wholesale Grocers' Assn.*, Complaint No. 894, Order issued May 23, 1924. A complaint against the *Philadelphia Wholesale Drug Co., et al.*, on similar charges was dismissed without any reasons being assigned, 4 F. T. C. 483 (1921). Commissioner Gaskill entered a vigorous dissent to this disposition of the case, 4 F. T. C. 491.

other connection in the series of reports of which this study is a part.<sup>1</sup>

#### §7. INTERLOCKING DIRECTORATES AND STOCK ACQUISITION IN COMPETING COMPANIES

Another subject of regulation by the Federal Trade Commission which is in no proper sense a business practice or method of competition is the question of corporate relations among competitors. Here, however, the Commission acts under an explicit mandate of Congress. Sections 7 and 8 of the Clayton Act respectively prohibit intercorporate stockholding and interlocking directorates between competitors under certain conditions; and the power to enforce these provisions, except with reference to banks and common carriers, is by Section 11 vested in the Federal Trade Commission.

The prohibition of interlocking directorates may be dismissed with brief consideration. Not until 1924, nearly ten years after the passage of the Clayton Act, was a complaint issued based upon an alleged violation of Section 8.<sup>2</sup> The two cases of this character now pending both relate to the service by individual respondents upon boards of directors of nominally competing California sugar refineries. If there should prove to be a technical violation of the Clayton Act in these cases, it will not alter the fact that the law is completely ineffectual. It offers no obstruction whatever to the establishment of a uniform policy for nominally independent and competitive enterprises through a common ownership of their stocks. Voting power of stocks held by one person in two or more nominally competing concerns is in no way disturbed. All that is necessary to comply with the law, therefore, is for the real owner to act through trusted representatives in exercising such power as his stock-holding may give him over the administration of the various enterprises in which he is interested. As this is not uncommon in any case, i. e., without respect to the competitive relationship of

<sup>1</sup> See National Industrial Conference Board, "Trade Associations: Their Economic Significance and Legal Status," New York, 1925, Chap. II.

<sup>2</sup> *S. W. Sinsheimer, et al.*, Complaint No. 1180. Annual Report, 1924, p. 234; *E. A. Carlton, et al.*, Complaint No. 1182. Annual Report, 1924, p. 234.

these several enterprises, particularly in the case of estates and of those possessing large capital, the utter inconsequence of this section of the Clayton Act for the purpose for which it was intended is apparent. But the law is not simply innocuous. It is, to a degree, harmful. For without affording any protection against monopolization or control of the market, it deprives industry and trade in many instances of the direct counsel of the most competent and best informed business leaders. Men who have a capacity to take an active share, directly and honorably, in the executive responsibility for certain corporations in which they have an interest are deterred from doing so by the fact that the products of such concerns may be more or less similar to those of other concerns in which they are interested, or that their market areas may to some extent overlap the market areas of such other concerns. To the extent that Section 8 interferes with the most capable management of the affairs of industrial corporations, there is ground for its repeal, since as it stands it accomplishes precisely nothing.

The prohibition of intercorporate stockholding among competing concerns appears to be not quite so ineffectual, but it may readily become far more injurious under a certain construction of which Section 7 is susceptible. The possibility that this section may be so construed has not yet been completely eliminated, moreover. The Clayton Act provides, in this section, that it shall be unlawful for one corporation to acquire stock in one or more other corporations "where the effect of such acquisition may be to substantially lessen competition between such corporations, or any of them." If this language were to be taken to mean what the words in ordinary usage would indicate, and if no account were taken of the exceptions mentioned in the same section, it would have to be concluded that it is absolutely unlawful under all circumstances for one concern to buy out or acquire an interest in an actual competitor in the same line of commerce by the purchase of its capital stock. Equally one must conclude that exactly the same end may be lawfully achieved by the simple expedient of buying the assets instead of the stock certificates which represent the proprietary interest in the assets of the identical competitor. Moreover, it would

likewise follow that the possession of any part of the capital stock of a competing corporation, held at the time of the enactment of the law, would not be affected by this section. Are these incongruous results forestalled by virtue of the exceptions referred to above?

The exceptions provide that: "This section shall not apply to corporations purchasing such stock solely for investment and not using the same by voting or otherwise to bring about . . . the substantial lessening of competition. Nor shall anything contained in this section prevent a corporation . . . from causing the formation of subsidiary corporations for the actual carrying on of their immediate and lawful business, or the natural and legitimate branches or extensions thereof, or from owning and holding all or a part of the stock of such subsidiary corporations."<sup>1</sup> These exceptions are undoubtedly important and under a sufficiently broad construction might, at least, make the Act workable (omitting from consideration for the moment the question of evasion), without at the same time destroying its effectiveness for the essential purpose for which it was enacted.

What was that purpose? Without attempting to recapitulate here the history of the 1914 legislation,<sup>2</sup> the statement will hardly be challenged that the plain intent of Congress in the Clayton Act was to frustrate attempts to monopolize any branch of trade or control any section of the interstate market by *prohibiting certain definite steps in that direction*. This last clause is italicized to emphasize the essential feature which distinguishes the Clayton Act from the Sherman Act. Aside from the fact that it makes independently unlawful several specified measures taken in furtherance of, or in an approach to unlawful monopoly, it does not differ from or add to the basic statute of 1890. If this be accepted as a sound view of the nature of the Clayton Act, it follows that the only policy in applying the seventh section consistent with the spirit and object of the whole Act must be to confine it to mergers of previously competing concerns, indicating a purpose as well as an imminent or actual power of suppressing competition in some line of commerce and estab-

<sup>1</sup> Act of October 15, 1914, 38 Stat. at Large 730, Section 7.

<sup>2</sup> See Chapter III, *supra*.

lishing a monopoly. Considering the statute as a whole and its relation to the Sherman Act, there seems no ground for condemning under its provisions every acquisition by one concern, no matter how small and insignificant a factor in the given line of trade it may be, of a controlling interest in another concern previously competing. Such transfers are very common, and usually bear no relation to competitive conditions in the general market. There would seem to be nothing in the statute, moreover, to hinder even a large combination from extending its productive operations into related fields of industry by acquiring stock control of some enterprise already established there.<sup>1</sup> Nor is there any prohibition against expansion into new markets, even by a large and dominant concern. There is nothing to prevent, for example, a firm producing a large percentage of the output of Georgia granite from opening a quarry in Vermont, or, if it prefers, buying up the capital stock of a corporation already operating in that region. In either case, there is no elimination of competition in the market for Vermont granite. Finally, there would seem to be considerations of sound policy for distinguishing between the union of independent producers in an industry already dominated by a large combination and the acquisition of independent concerns by that combination. The reduction of the number of competitors in the former case might well tend to equalize the strength of the remaining contestants.<sup>2</sup>

Have these various considerations found expression in the policy of the Federal Trade Commission? Or has it attempted to interfere in transactions amounting to nothing more than the natural and legitimate expansion of a prosperous enterprise? And what attitude have the courts taken towards the scope of the regulative power in this particular? Is the test for violation of Section 7 of the Clayton Act the

<sup>1</sup> The acquisition by a quasi-monopolistic enterprise of a controlling interest in a concern producing a substitute article might substantially lessen competition provided the concern acquired was an important factor in its field.

<sup>2</sup> In this connection should be noted the complaints against the post-war mergers in the steel industry. Complaint No. 891, *Bethlehem Steel Corp. & Lackawanna Steel Co.*; Complaint No. 905, *Midvale Steel & Ordnance Co., Republic Iron & Steel Co., and Inland Steel Co.*; Complaint No. 962, *Bethlehem Steel Corp.* The first two complaints have been dismissed, Annual Report, 1923, p. 217. The latter case is pending, Annual Report, 1924, p. 208.

same in substance as the test for a violation of Section 2 of the Sherman Act? Or is the test the lessening of the competition between the corporations one of which acquires stock in the other, even when such purchase is made "solely for investment," or for "natural and legitimate branches or extensions?"

Approximately thirty complaints have been issued by the Federal Trade Commission charging unlawful acquisition of the control of competitors. Seven of these have been dismissed,<sup>1</sup> and six orders to cease and desist have been issued.<sup>2</sup> About twenty cases are pending.<sup>3</sup> As the dismissals are made without any, or only a perfunctory, explanation, there remains only the rather narrow base of five adverse orders upon which to determine the outline of administrative policy in this field. Oddly enough, appeal has been taken to the courts from each of these five orders. This circumstance will contribute to the clarification of what is the administrative and what the judicial conception of the proper scope of this section of the Clayton Act.

In every instance the findings of fact set forth that the respondent and the acquired company were in active competition prior to the acquisition. In two cases only are figures given showing the percentage of the total product for the given market area affected produced or sold by the respective parties;<sup>4</sup> but in one other case it was found that the respondent company possessed an absolute monopoly of the domestic market for the principal raw material used by

<sup>1</sup> Complaint No. 92, *Standard Oil Co. of N. Y.*, 2 F. T. C. 465 (1920); Complaint No. 250, *Borden's Farm Products Co.*, 5 F. T. C. 482 (1922); Complaint No. 751 *Crystal Ice & Storage Co.*, 4 F. T. C. 485 (1922); Complaint No. 891, *Bethlehem Steel Corp., et al.*, 5 F. T. C. 488 (1923); Complaint No. 905, *Middvale Steel & Ordnance Co.*, 5 F. T. C. 487 (1922); Complaint No. 1022, *Hygrade Lamp Co.*, dismissed October, 1924; Complaint No. 745, *Austin, Nichols & Co.*, Dismissal announced, May 26, 1925.

<sup>2</sup> *Aluminum Co. of America*, 3 F. T. C. 302 (1921); *Armour & Co.*, 4 F. T. C. 457 (1922); *Swift & Co.*, 5 F. T. C. 143 (1922); *Western Meat Co.*, 5 F. T. C. 417 (1923); *Thatcher Mfg. Co.*, 6 F. T. C. 213 (1923); Complaint No. 1023, *International Shoe Co.*, Order issued, July 29, 1925.

<sup>3</sup> Of which six have been initiated in the nine months since June 30, 1924.

<sup>4</sup> *Armour & Co.*, 4 F. T. C. 457, 460-461; *Thatcher Mfg. Co.*, 6 F. T. C. 213, 240. In the former case, figures are given upon the sales of branch houses of Armour & Co. in Spokane, Portland and Butte. The acquired company, E. H. Stanton Co., was found to have sold about 75% of the meat and meat products in Spokane and surrounding territory. In the Thatcher case, the respondent was shown to have been the largest producer of milk bottles in the United States. Its output for 1918-21 is given, together with the output of each of the acquired companies in 1919.

the company acquired.<sup>1</sup> It appears, however, that the three cases against packing houses were all similar, in that flourishing local meat packing companies were bought out by the respondents, well known as national packers and distributors of meat products. In the two cases against Swift and Company, the respondent in the Western Meat Company case being a mere subsidiary of that organization, the findings do not indicate, however, the extent of Swift and Company's prior participation in the meat trade of the districts in question, nor whether any substantial independent local production remained. It is possible that the Commission took evidence on these points, but aside from the general reputation of the so-called "Big Five" packers, there is no basis upon which it could be concluded that competitive conditions were destroyed by the transactions in question. In the proceedings against the Aluminum Company of America and the Thatcher Manufacturing Company the dominating position of the respondents in their respective industries was clearly shown in the manner indicated above.

So far, the decisions in the courts have upheld the Commission upon the vital points in the appealed orders.<sup>2</sup> In both the Aluminum case and the Western Meat Company case the courts found that the evidence supported the conclusion of the Commission that there had been a violation of Section 7 of the Clayton Act. But the two circuit courts of appeals have taken evidently contradictory positions relative to the legitimacy of evasion of the law by purchase of assets instead of by acquisition of stock. The court in the third circuit refused to credit the scheme of the Aluminum Company of America for getting around the law as a bona fide transaction. The petitioner contended that by forming a new company, the Aluminum Rolling Mills Company (for two-thirds of the stock of which it subscribed), which purchased certain physical properties of the Cleveland Metal Products Company, a competitor of petitioner, it had complied with the law. It was argued that at the time the stock

<sup>1</sup> *Aluminum Co. of America*, 3 F. T. C. 302 (1921). The respondent in this case also engaged in the manufacture of sheet aluminum into aluminum utensils, but its relative position in this branch of the trade is not stated.

<sup>2</sup> *Aluminum Co. of America v. Federal Trade Commission*, 284 Fed. 401 (1922); *Western Meat Co. v. Federal Trade Commission*, 1 Fed. (2d) 95 (1924).



of the Aluminum Rolling Mills Company was acquired that company was not yet manufacturing aluminum products, and therefore was not a competitor of the respondent. "It seems to us that in this defense," said the court, "the Aluminum Company stands on a ledge too narrow for safety."<sup>1</sup> The court then analyzed the entire transaction, and rendered a judgment sustaining in full the order of the Commission.

The court in the ninth circuit, on the other hand, has clearly shown its conviction that the technical form of the transaction is the essence of what was condemned in the seventh section of the Clayton Act. After having denied the petition of the Western Meat Company to vacate the order of the Federal Trade Commission requiring the respondent to divest itself of all interest in the illegally acquired concern, the court upon a rehearing consented to modify the Commission's order.<sup>2</sup> Not changing its view that respondent had violated the law, the court stated its opinion that the order exceeded the Commission's authority in requiring the petitioner to dispose not only of the former competitor's stock but of the plant and equipment as well. The decree of the court expressly sanctions the retention of the property, if the stock (after the assets have been alienated to its present owners, of course) is returned to the parties from whom it was purchased.<sup>3</sup>

This conflict of construction between the circuit courts of appeal goes to the heart of the statute in question. If the view of the court for the ninth circuit prevails, only in cases in which it is impossible to secure the consent of all stockholders to the sale of the assets of the company sought to be acquired will the law continue to have any effect. The attitude of the Supreme Court upon this issue cannot be forecasted, for so far its sole action touching the matter has been the refusal of a writ of certiorari in the Aluminum Company case.<sup>4</sup>

<sup>1</sup> 284 Fed. 410.

<sup>2</sup> *Western Meat Co. v. Federal Trade Commission*, 4 Fed. (2d) 223 (1925).

<sup>3</sup> *Ibid.*, p. 225. "The order of the Federal Trade Commission will be so modified as to eliminate therefrom the injunction against the acquisition by the petitioner of the plant and property of the Nevada Packing Company." The Federal Trade Commission has appealed from this ruling. Petition filed May 1, 1925.

<sup>4</sup> *Aluminum Company of America v. Federal Trade Commission*, 261 U. S. 616 (1923).

## CHAPTER VII

### PUBLIC POLICY AND BUSINESS STANDARDS

In reviewing the effort of the government to safeguard the competitive process in the fields of manufacture and trade, two distinct questions invite attention. There is, first, the question of the scope of government regulation. What features of business administration are subject to control, and how far may authoritative interference in business properly extend? This question of the substance or reach of coercive control of business methods has been discussed in detail in the foregoing chapters. It will require only summary treatment by way of conclusion. The second question which suggests itself in a survey of the government policy in this field relates to administrative technique. How are the measures of government regulation, whatever their character, to be made effective? The discussion of this aspect of the regulatory power of government, particularly as related to the activity of federal agencies, will occupy the chief portion of this concluding chapter.

#### §1. THE SCOPE OF GOVERNMENT REGULATION

It has been clearly indicated in the course of the inquiry in the preceding pages that the judicial regulation of competitive methods under the common law was inadequate to cope with all of the innovations to which changes in the modern commercial structure gave rise. The judicial process could, in the first place, be invoked only by the injured party who was the direct object of attack,—except in those rare instances of resort to the grosser forms of competitive rivalry subject to criminal prosecution. The public interest in fair competition and upright business conduct found no responsible defender. Moreover, a variety of new abuses were rapidly developing which could be brought within the

stereotyped doctrines of the common law only with difficulty, if at all. The growing range of substitute commodities, the increasing importance of advertising in market distribution, the multiplication of brands, the extensive development of patents, and the concentration of the control of numerous lines of industry—these represent some of the manifold factors in the business situation which have helped to make the competitive process susceptible of perversion. The growth of voluntary protective and educational organizations among business men and an increasing recognition of the dependence of continued business success upon the good-will of consumers have done much to counteract the tendencies to abuse which reside in a rapidly changing commercial and industrial environment. But such forces did not dispense with the need for some measure of coercive regulation. They operate, from their very nature, only very slowly, and take effect unevenly over the entire field of business.

In the sphere of interstate commerce,<sup>1</sup> the Federal Trade Commission was instituted as the agency for preventing an insidious undermining of the competitive régime by predatory or unfair tactics developing out of such transformations as have been described. The prohibitions of the Clayton Act and the Trade Commission Act, which the Commission was authorized to enforce, were professedly supplementary to the Sherman Act. The Federal Trade Commission was given no mandate to participate in any degree whatever in the responsible management of private industrial and commercial enterprises. Where the issue in regard to any practice is simply as to whether or not it is economically sound, whether or not it tends to promote the general prosperity or national welfare, it is beyond the scope of the Federal Trade Commission's jurisdiction, and properly so. Neither Congress nor any considerable section of the American public has evinced any disposition to withdraw from the discretion of

<sup>1</sup>The nature of this study precludes a discussion of the intricate legal issues surrounding this constitutional limitation of the Federal Trade Commission's authority. The reversal of the Commission's orders in the ship chandlery cases on the ground that interstate commerce was not involved has already been noted. Other cases in which this issue has been raised and determined adversely to the Commission's jurisdiction, at least in part, are: *Ward Baking Co. v. Federal Trade Commission*, 264 Fed. 330 (1920); *Pacific States Paper Trade Association v. Federal Trade Commission*, 4 Fed. (2d) 457 (1925).

private citizens and place under the influence of a bureaucratic body the determination of questions purely of economic expediency in the management of industry and commerce. The functions of the Federal Trade Commission in this respect are sharply contrasted with those of the Interstate Commerce Commission. Dealing there with a special class of industries, particularly common carriers, Congress has authorized the Interstate Commerce Commission to assume a responsible rôle in the determination of their rates, services, and like features of business policy. No such authority has been granted the Federal Trade Commission, however, or seems likely to be.

Nevertheless, in the exercise of its administrative powers the Commission appears occasionally to have lost sight of this fundamental limitation upon its functions.<sup>1</sup> This has been shown in numerous instances in the course of this inquiry. It need only be observed here that, in attempting to establish a minimum standard for price making and in attempting to prohibit the guarantee against price decline, the policy of the Commission seems plainly to have exceeded the scope of its mandate. In most such matters, however, it may be safely ventured upon the record of judicial appeals already considered, that the courts will in due course furnish a simple and sufficient corrective. The general lines upon which this delimitation of the Federal Trade Commission's jurisdiction may well be drawn have been sketched in connection with the criticism of the several species of regulation which have been attempted.

In the main, it may be concluded, administrative regulation as it has developed during the past decade represents a constructive force in keeping the fields of industry and trade open to the spontaneous growth of free enterprise. To the

<sup>1</sup> The failure of the Commission to render opinions in support of its orders, or in explanation of the dismissal of complaints without orders, makes it difficult to determine precisely the view of its jurisdiction taken by the Commission. This can only be deduced from a comparison of its findings and orders in a number of cases.

The Commission has been criticized for this failure to declare the grounds for its action in specific cases. See G. C. Henderson, "The Federal Trade Commission," New Haven, 1924, pp. 105-112, 333-337. While much might be gained in this way in clarifying administrative action in particular cases, it may be pointed out that the closer approximation to judicial procedure and the resultant tendency towards the development of stereotyped precedents might in a measure be a handicap upon the Commission.

courts, however, must be attributed much of the credit for this accomplishment of the launching of the Federal Trade Commission upon a fairly even keel. The new craft has tended at times to list heavily, but the gyroscopic action of judicial review, wisely provided by Congress as an integral part of the administrative machinery, had preserved the ship's balance. It is not so much in the lines of regulation which the Federal Trade Commission has undertaken that its policy may be in need of criticism as in the failure to formulate definite standards of what constitutes a basis for procedure in respect to each type of questionable business practice. Only when there has been a clear enunciation of the essential principles underlying the intervention of the Commission in each class of cases will the Commission be able to introduce consistency into its procedure and avoid the issuance of egregious complaints.

The courts, as indicated above, have advanced this necessary process of formulating precise and explicit principles for the guidance of administrative action to a considerable degree. In not all instances does it seem possible to agree that these principles have been wisely conceived, notably in respect to the Commission's jurisdiction over conspiracies in restraint of trade. There is need, moreover, of still further definition, and equally of a thorough and continuous critical examination of such definition as it proceeds. This latter need the previous chapters of this report are intended in some measure to supply. It may be explained, though explanation should hardly be required, that this process of definition in no way conflicts with the preservation of that elasticity in the law which is so essential to effective administrative regulation, and which was recognized by Congress in the broad terms of the fifth section of the Federal Trade Commission Act. Elasticity is provided by the power to reach new abuses not comprehended within the classes of practices previously condemned, to reach new forms of old evils, and, finally, to exercise a wholesome discretion in determining whether the facts of a given case warrant the application of disciplinary measures. Not elasticity but confusion results from vagueness in respect to the essential elements constituting an offense under the law.

## §2. PROBLEMS OF ADMINISTRATIVE PROCEDURE

The second general question to which attention must be directed in any comprehensive review of the experience of the last decade in the federal regulation of business practices is the question of administrative technique. The commission method of regulation introduces peculiar problems with respect to the combination of governmental functions, the extent of administrative power over persons or corporations subject to regulation, the publicity surrounding proceedings, and the like. The institution and development of the Federal Trade Commission have exhibited the difficult adjustments which such problems require. In particular, the exercise of the executive function of a prosecutor and the judicial function of a court by the Commission in the same cases has been criticized as inimical to the fair consideration of the interests of respondents. It is represented that the fallacy of combining two such incompatible rôles in one body is reflected in the record of appealed orders, which shows the Commission to have been upheld in approximately one-third of the cases appealed.<sup>1</sup> Is it to be concluded that the functions of prosecutor and judge are entirely distinct and incompatible? What is, in fact, the essential nature and proper function of the Federal Trade Commission? An answer to these questions may afford some basis for constructive criticism of the methods of procedure of the Commission, which have latterly been the subject of sharp controversy.

<sup>1</sup>Of a total of 55 appeals from the orders of the Commission from its establishment to June 30, 1924, one had been withdrawn and 40 finally disposed of prior to that date. In 26 of these cases, the Commission's ruling had been either reversed or modified, while in 14 instances the courts had sustained the Commission. In considering whether and how far this record is discreditable, there should be set over against the relatively large number of reversals, in whole or in part, the relatively small number of appeals from the rulings of the Commission. Of the 635 orders to cease and desist issued prior to June 30, 1924, some 580 were accepted as binding by the respondents. In one sense, it is proper to say, therefore, that the Commission has been overruled in only 4 per cent of its decisions, instead of 65 per cent, based on appealed cases. See Annual Report, 1924, pp. 62-63. This takes no account, however, of the numerous orders which have, in effect, been invalidated by subsequent adverse judicial decisions in substantially similar cases, as, for example, some fifteen of the orders in the oil pump proceedings which were not appealed. See, *ante*, Chapter VI, Sect. 5. The exact number of orders thus affected it is not possible to determine. It may be noted that the Commission has in some instances formally rescinded prior orders under such circumstances, e. g., in the case of the *South Bend Bait Co.*, Complaint No. 729, Annual Report, 1924, p. 191. Why it has not done so in other cases, thereby following a consistent policy, is difficult to understand, and no explanation has ever been given by the Commission.

## §3. DUAL FUNCTION OF FEDERAL TRADE COMMISSION

That the Federal Trade Commission does combine an executive function and a judicial function is indisputable. It is authorized, as no court is authorized to do, to act on its own initiative in conducting investigations and, if the facts appear to it to warrant, instituting corrective proceedings in the public interest against supposed commercial malefactors. At the same time it has a quasi-judicial character. It possesses discretionary power to interpret the law as applied to a given set of facts, after having found those facts from the evidence which it has full power to elicit at formal hearings by customary judicial processes. The Commissioners are, thus, in many respects judges. In this duality of function there is, however, nothing unique or peculiar. The ancient fiction that it is possible to maintain three separate and independent branches of government, each scrupulously avoiding any incursion into the essentially distinct functions of the others, has long since been dissipated.<sup>1</sup> It is not necessary to restrict citations for proof of this to the numerous administrative agencies which, like the Federal Trade Commission, are expressly endowed with some combination of judicial, executive, and legislative functions. The Bureau of Internal Revenue with the Secretary of the Treasury at its head, the Bureau of Pensions and the National Park Service under the Secretary of the Interior, and the independent Interstate Commerce Commission, the United States Tariff Commission, and the Federal Reserve Board, to mention no others, all illustrate various combinations of these governmental functions.<sup>2</sup> The truth is that in practice it is impossible entirely to divorce them. When a legislature enacts or declines to enact a law providing for compensation to some citizen injured by a governmental

<sup>1</sup> Even in 1842 the Supreme Court felt justified in pointing out that, "The executive, in acting upon claims of service rendered, may be said to exercise, if not in form, in substance, a judicial power. And so a court, in the use of a discretion essential to its existence, by the adoption of rules, or otherwise, may be said to legislate. A legislature, in providing for the payment of a claim, exercises a power in its nature judicial, but this is coupled with the paramount and remedial power." *Watkins v. Holman*, 16 Peters 25, 60.

<sup>2</sup> For a general survey of the judicial discretion exercised by federal administrative officers, see: Gregory Hankin, "Conclusiveness of the Federal Trade Commission's Findings as to Facts," 23 *Michigan Law Review*, 233-272 (1925).

agency it occupies a judicial rôle which the courts have vacated by virtue of the non-suability of sovereign states. When a judge determines that a rigid common law doctrine fits or does not fit a new situation, which in spirit it covers but as previously formulated for other sets of facts it excludes, he is exercising a legislative function—fixing a rule of conduct for the premises. When a prosecuting attorney decides to bring on information against a party accused of a crime he weighs the evidence before him and passes upon its sufficiency after the manner of a court of law. His decision, of course, is not definitive but it has, nevertheless, serious consequences for the supposed offender.

There is nothing exceptional, therefore, in the grant of a combination of judicial and executive functions to the Federal Trade Commission. The criticism of the Commission on this score appears to have arisen from a misapprehension of its primary purpose. Properly regarded, the Commission's judicial functions are merely auxiliary or incidental to its investigational and administrative functions. It is fundamentally a fact-finding body, empowered to eliminate trade abuses which it discovers, either by simple command, if the offenders are willing to comply, or by prosecution if they resist. Its critics, on the other hand, are inclined to treat it as a court rather than as an administrative tribunal. Several circumstances appear to have contributed to this misplaced emphasis. First and foremost, the Federal Trade Commission Act itself provided that "the findings of the Commission as to the facts, if supported by testimony, shall be conclusive."<sup>1</sup> It thereby made a hearing before the Commission in this respect a trial of the case. Moreover, in issuing an order upon the basis of its findings of fact the Commission necessarily interprets the law and, in a formal sense, applies it to the situation revealed by the evidence. But there the analogy to the judicial process ceases. The final and decisive feature of judicial procedure is lacking. The Commission cannot itself enforce its orders. They are decrees without sanctions. The failure to provide for the imposition by the Commission of penalties for disregard of its orders was not a Congressional oversight. The power of enforcement was deliberately reserved to the courts. Why

<sup>1</sup> 38 Stat. at large, 717, Section 5.



was this done? For the obvious reason that in case of any question about the meaning of or scope of the law, the legal issue was for the courts to determine. Before any administrative order could become effective against the will of a respondent, therefore, it was provided that there should be a judicial determination of whether the facts found constituted a violation of law.

#### §4. EXPERIENCE OF INTERSTATE COMMERCE COMMISSION

The scheme of procedure thus provided was based upon experience. For nearly twenty years the Interstate Commerce Commission struggled futilely to obtain recognition as a body of experts whose findings and rulings in the determination of such difficult and technical questions as what constituted an unjust discrimination or an unreasonable rate should carry some weight. But as long as its rulings were considered merely as *prima facie* evidence of the facts its procedure was largely ineffective. Appeals to the courts opened up each case anew and the courts, although admittedly without expert qualifications, were required to interpret the facts as well as interpret the law in every proceeding. Many significant orders, therefore, became tangled up immediately in litigation which frequently extended over three to six years and sometimes even longer.<sup>1</sup> Much of the advantage from the summary character of administrative proceedings was thus forfeited. As early as 1890 the Interstate Commerce Commission in its Annual Report<sup>2</sup>

<sup>1</sup> W. Z. Ripley, "Railway Rates and Regulation," New York, 1913, pp. 460-461.

<sup>2</sup> Fourth Annual Report of Interstate Commerce Commission (1890), pp. 10-11. In the course of its argument, the Commission declared: "If a carrier can simply ignore the findings of the Commission and wait for a new trial in the courts upon different testimony, in a proceeding to be instituted and carried on by the Commission, there can be no certainty upon any administrative question until the judgment of the court of last resort shall be pronounced and the delay substantially defeats the remedy. This is fatal to effective regulation. The remedial procedure should be in a measure summary, and there must be finality, so far as facts are concerned, in the action of some tribunal, leaving only questions of law for review, and these at the instance of the party claiming to be aggrieved. A procedure of this nature would be in harmony with the general policy of the law that the facts, as found by the primary body that hears the testimony and sees the witnesses, shall be final for purposes of justice and for appellate review. . . . It is, of course, possible that erroneous findings may sometimes be made by the Commission, but in all such cases corrections are feasible, on proper showing, by the Commission itself. Moreover, error is predicable of any tribunal, and the probabilities of error upon questions of fact are not diminished by the remoteness of the final tribunal from the forum in which those questions are originally litigated."

urged upon Congress the wisdom of the change which was finally brought about by the Hepburn Amendment of 1906. The fifteenth section of the Interstate Commerce Act, as amended, had the effect of making the Commission's conclusions of fact reviewable only within narrow limits.<sup>1</sup> The nature of this change was described by the Supreme Court in a leading case as follows:

"Originally the duty of the courts to determine whether an order should or should not be enforced carried with it the obligation to consider both the facts and the law. But it had come to pass (after 1906) that in considering the subject of orders of the Commission, for the purpose of enforcing or restraining their enforcement, the courts were confined by statutory operation to determining whether there had been violations of the Constitution, a want of conformity to statutory authority, or of ascertaining whether power had been so arbitrarily, exercised as virtually to transcend the authority conferred although it may not be technically doing so."<sup>2</sup>

This experience of the Interstate Commerce Commission undoubtedly weighed heavily with Congress in outlining the procedure of the Federal Trade Commission. It had been clearly demonstrated that unless the findings of an administrative body were made conclusive its hearings would amount to nothing more than preliminary inquiries to determine whether prosecution in the courts should be instituted. The Commission could be sorely embarrassed by the suppression of important defensive evidence, and the regulative process simply prolonged by the period required for a hearing.

#### §5. THE PURPOSE OF ADMINISTRATIVE PROCEDURE

This explanation of the procedural provisions of the Federal Trade Commission Act, giving the Commission power to conduct formal primary hearings, making its find-

<sup>1</sup> See: 34 Stat. 584, c. 5891, Sect. 15. In *I. C. C. v. Union Pacific R. R. Co.*, 222 U. S. 541 (1912), the Supreme Court announced the rule which still obtains. "In determining these mixed questions of law and fact, the court confines itself to the ultimate question as to whether the Commission acted within its power. . . . Its conclusion, of course, is subject to review, but when supported by evidence is accepted as final; not that its decision, involving as it does so many and such vast public interests, can be supported by a mere scintilla of proof,—but the courts will not examine the facts further than to determine whether there was substantial evidence to sustain the order." Pp. 547-548.

<sup>2</sup> *Proctor & Gamble Co. v. U. S.*, 225 U. S. 282, 297-8 (1912).

ings of fact not presumptive but conclusive, but withholding any power of enforcement of its orders without judicial review of the applicability of the law to the facts found, shows that the character deliberately given the Commission was neither that of a court, on the one hand, nor of a grand jury, on the other. The purpose, founded on abundant experience, was to secure for the administrative regulation of competitive methods the advantages of summary procedure, a flexible and elastic adjustment of the law to the manifold changes and varieties of business practice, the consideration of trade usages and commercial policies in the light of the broad experience of a body of trained experts, and the unification of government regulative policy through centering responsibility for enforcement of the law in a single body—these advantages were to be secured, if possible, without sacrificing that fundamental principle of American political life that there must be a “government of laws and not of men.” In particular, the penalties of the law were to be inflicted on no one without opportunity being afforded for a judicial determination of the legitimacy or illegitimacy of any given line of conduct. At the same time, experience had shown that in undertaking any such course of regulation as that aiming at fairness in trade competition there are a great number of cases bound to come up which clearly contravene definite and traditional standards of integrity and fair-dealing. The appeal of such cases to the courts by respondents is recognized on all sides to be futile. Nothing more is needed for the suppression of such practices than effective publicity and a warning notice from some responsible authority. Summary procedure by a Commission, quasi-judicial in character, may serve to prevent the further crowding of court dockets attendant upon the creation of new offenses while the safeguards of legal justice are in no way impaired. It was upon this theory that the Federal Trade Commission was instituted, and it is error to look upon the Commission as a special court responsible for the interpretation of certain statutory law.

If, in practice, these advantages of commission regulation have not been completely realized, it is worth considering, nevertheless, what has been accomplished. Taking the

ten-year record in its entirety, the Commission had taken under advisement 8,632 requests for action to prevent unfair competition. Of these, 3,591 had been filed as applications for complaint, thereby becoming the subject of official investigation, while 4,727 had been definitely rejected summarily, as for lack of federal jurisdiction or similar cause. Out of the total of 3,591 formal applications the Commission had dismissed 2,058 after investigation, and issued complaints in 1,197 cases. There had been 933 complaints finally disposed of, 635 of which had resulted in orders to cease and desist. The most striking characteristic of this mass of cases is, perhaps, the comparative obscurity of the great majority of the respondents. One may glance over scores of titles without finding the name of a single corporation nationally known. Complaints have occasionally issued against large corporate consolidations, but by far the most of the orders have been directed to firms of moderate size and abbreviated lineage. Often partnerships or individual traders are the respondents. This circumstance, coupled with the fact that only 8.6 per cent of the orders had been appealed to the courts, tends strongly to confirm the view that there is a place in our government economy for an administrative tribunal with summary procedure to warn transient business concerns against the use of fraudulent and predatory tactics.

Another feature of the ten-year record of the Federal Trade Commission tends to indicate, however, that this function is not being performed with that dispatch which is imperative for effectiveness. The number of complaints pending at the beginning of each fiscal year tended steadily to mount up to 1923, and has remained since then at a comparatively high level, around 250 each year. This would seem to indicate a pronounced incapacity, upon the basis of the available personnel and equipment, to handle the volume of work which the Commission is called upon to perform.<sup>1</sup> More significant still is the slowness of its pro-

<sup>1</sup> In this connection, it should be noted that the investigational work of the Economic Division, which consumes a considerable part of the appropriations as well as of the attention of the Commission, has also tended to lag behind its program. For the fiscal year ended June 30, 1924, the expenditures on account of the Economic Division were nearly half those made in connection with legal procedure. Annual Report, 1924, p. 6.

cedure, which, in a measure, reflects this same circumstance, of course. An examination of the records of the 123 cases<sup>1</sup> finally disposed of during the fiscal year ending June 30, 1924, reveals an average pendency of 22 months and 6 days.<sup>2</sup> This period is exclusive of the time taken for preliminary investigation, of which there is no available record; but there are indications that it varies from a few weeks to several months. In the total of 123 cases disposed of, moreover, there was one dismissal in which the elapsed time from complaint to final disposition was exactly six years, and a group of seventeen orders to cease and desist issued four years, three months, and seven days after the filing of the complaint. None of these, apparently, was held up by any consideration of issues pending adjudication in the courts. Certainly from the point of view of expedition, Federal Trade Commission procedure leaves much to be desired.

#### §6. SUGGESTIONS FOR LIMITING SCOPE OF COMMISSION'S ADMINISTRATIVE RESPONSIBILITY

The accumulating mass of unfinished work and the vexatious delay in the disposition of complaints cannot all be ascribed to the handicap of an inadequate force. In some directions the Commission appears to have exerted its powers where it was charged with no responsibility and in other directions it seems possible to limit its responsibilities without any sacrifice of the objects for which the Commission was established. This aspect of the shortcomings of the existing system of administrative regulation leads to some suggestions

<sup>1</sup> This computation excludes five cases in which orders to cease and desist previously issued were rescinded. The Commission counted these as ordinary dismissals, but it is clear that these cases are not comparable, for the purpose in hand, to the final disposition of original proceedings.

<sup>2</sup> The cases resulting in orders to cease and desist, 92 in number; were pending an average period of 20 months and 18 days; while those resulting in dismissals were pending an average period of 26 months and 23 days.

It appears from a comparison of these figures with the figures obtained by Mr. G. C. Henderson, showing the elapsed time of 479 cases, decided prior to June 30, 1921, that there has been no tendency toward an acceleration of Federal Trade Commission procedure. Indeed, the indications are quite the reverse. Of the cases examined by Mr. Henderson, the 360 resulting in orders to cease and desist had an average pendency of 7 months and 11 days. The remaining 119 cases, which resulted in dismissals, were pending an average period of 20 months and 18 days. See G. C. Henderson, "The Federal Trade Commission," *op. cit.*, p. 89.

of legislative reform. It has already been advanced that the Federal Trade Commission is not the proper agency for prosecuting conspiracies in restraint of trade. Such combinations are unlawful under the Sherman Act and subject to its penal provisions. Congress did not intend to place the responsibility for the enforcement of the Sherman Act upon the Federal Trade Commission, and it obviously does not belong there. But, as has been observed, the Commission has assumed jurisdiction in numerous conspiracy cases under Section 5 of its foundation act, and has been upheld in this action by the courts. It seems necessary, therefore, in order to bring about a more logical and efficacious distribution of functions, and thereby contribute to the expedition of Federal Trade Commission procedure in its proper sphere, to provide by law that whenever the Commission secures evidence pointing to a violation of the Sherman Act it shall transmit the same to the Department of Justice, with such recommendations as it may deem suitable. There is nothing to prevent the Commission from doing that now, of course. But it should be made mandatory in order to emphasize that the responsibilities of the Federal Trade Commission and the Department of Justice are neither coordinate nor overlapping.

In the second place, it should be possible to limit the responsibility of the Federal Trade Commission by a consolidation of the anti-trust sections of the Clayton Act with the Federal Trade Commission Act. This would tend to relieve the Commission of its present unmanageable burden in several ways. It would simplify greatly the task of interpreting substantive rules of law, which as they now stand contain a confusing jumble of technical and inconsequential, if not meaningless, phrases and passages. It has already been noted that in recent years the Commission has found ample authority under Section 5 of its organic act to reach offenses covered by the second and third sections of the Clayton Act. There is nothing to be lost and something to be gained, therefore, by the omission of these sections altogether in the process of legislative consolidation. It has also been suggested that both Section 7 and Section 8 of the Clayton Act, as it now reads, are either quite inefficacious or, upon another possible construction, pregnant with most pernicious conse-

quences. In the process of consolidating the anti-trust provisions of this statute with the Federal Trade Commission Act, these defects could be eliminated. But most important of all the considerations bearing upon the advisability of such a statutory consolidation is the extension of the private remedies afforded by Section 4 of the Clayton Act to persons injured by methods of competition found unfair under the fifth section of the Federal Trade Commission Act. Such a measure would tend to relieve the Commission of the responsibility of instituting proceedings in a great many cases, in which, at present, the complaining party has no adequate interest in bringing a private suit for damages, even if he has a right of action. It would automatically reduce the number of applications for complaints without in any way impairing the effectiveness of the law. Indeed, the dread of a severe penalty (triple damages) for engaging in an unfair method of competition should prove to have a salutary influence in deterring deliberate malfactors. And as it is necessary under both Section 7 of the Sherman Act and Section 4 of the Clayton Act, as judicially construed, for the plaintiff to prove special damages, there should be little danger of vexatious litigation or unmerited recoveries.<sup>1</sup>

#### §7. DISCRETIONARY POWERS OF FEDERAL TRADE COMMISSION

But even if the handicaps represented by insufficient resources, by a too ambitious extension of the field of regulation, and by the inexpert draftsmanship exhibited in the Clayton Act, were all removed, it is doubtful, judging from experience, whether Federal Trade Commission procedure would demonstrate then that swiftness and flexibility which are supposed to be the prime attributes of the administrative method. The Commission was endowed by its organic act with wide discretionary powers. If this discretion were exercised with a suitable combination of courage and moderation, of wisdom and prudence, it would undoubtedly enable the Commission to avoid much of the criticism which has been levelled at its slow technical procedure and rigid legalis-

<sup>1</sup> See *Keogh v. Chicago & Northwestern Ry. Co.*, 260 U. S. 156 (1922).

tic interpretation of the statutory prohibitions. The words of the statute are: "Whenever the commission shall have reason to believe that any . . . corporation has been or is using any unfair method of competition in Commerce, *and if it shall appear to the commission that a proceeding by it in respect thereof would be to the interest of the public*, it shall issue and serve upon such . . . corporation a complaint. . . ."<sup>1</sup> It is evident, thus, that the presence of a public interest is a condition precedent, quite independent of the condition that there shall be reasonable grounds for believing that the party accused has violated the law. In other words, the Commission is plainly empowered to refuse to act even when there is evidence that might, after hearing, support an order to cease and desist. But this is peculiarly a characteristic of an administrative body. A court is not endowed with a discretion to entertain or decline to entertain a bill or a complaint simply because in the view of the court the proceedings may or may not tend to promote the general welfare. If there is a cause of action stated, or if an information alleges a violation of law, a court must, from its very nature, stand ready to hear the case, no matter how trivial it may regard the rights or interests involved, or how excusable it may regard the conduct complained of. It is plain from the statutory provision quoted that what Justice Brandeis has called the "prophylactic action" of the Commission was uppermost in the minds of its creators. It was not designed to conduct a Sherman campaign in Georgia. It was designed as a "reconstruction mission."

Nevertheless, the Commission has not in practice adhered to such a policy consistently. It appears frequently to have ignored the broad discretion given it to avoid instituting proceedings not in the public interest. For example, when a small storekeeper in the city of Washington adopted the name "Shade Shop" in simulation of another retailer's business; the Commission set its organization in motion to restrain him, later appealing to the courts for enforcement of its order.<sup>2</sup> Recently, however, announcement has been made

<sup>1</sup> 39 Stat. 717, Section 5. Italics not in original.

<sup>2</sup> *Alfred Klesner*, 5 F. T. C. 24 (1922). It is not implied that every case of simulation of a competitor's name or product in which the complaining party may have a private right of action in the courts is devoid of the requisite public interest. The



of important changes of policy which seem to manifest a clearer recognition of the significance of the discretion granted in the "public interest" clause. In March, 1925, the Commission made a public declaration to the effect that, "Hereafter it shall be the policy of the Commission not to entertain proceedings of alleged unfair practices where the alleged violation of law is a purely private controversy redressable in the courts, except where said practices substantially tend to suppress competition as affecting the public."

The carrying out of this policy should mean a more precise definition of what constitutes an adequate public interest to justify the issuance of complaints. Prior to the adoption of this rule, as the statement itself implies and as a dissenting minority in the Commission has pointed out and contested, it seems to have been regarded as sufficient, in the preliminary examination of an application for a complaint, to establish reasonable grounds for a belief that an unfair method of competition had been practised. The record of the Commission amply justifies the announcement of a closer scrutiny in the future of the situation upon which a complaint is sought to be predicated, in advance of its issuance, to determine the existence of a genuine public interest in proceedings at the public expense. If there is no actual or potential menace to free enterprise or competitive markets there is no warrant, under the law, for federal interference. One test, for instance, which might be applied under this principle would relate to the scope of the business operations of the proposed respondent, and the prevalence in the trade of the given practice. Isolated instances of unfair competition practised by relatively insignificant concerns scarcely merit the expenditures necessitated by Federal Trade Commission action, particularly where competing private interests, recognized by law, rather than public interests, are mainly affected.<sup>1</sup>

wide distribution in interstate markets of package products resembling in appearance the containers of the products of a competing manufacturer presents quite a different case. Cf. *Best Oil Co.*, 5 F. T. C. 92 (1922).

<sup>1</sup> As, for example, in the proceedings against the L. B. Silver Co., involving the correct designation of a breed of hogs. See opinion in *L. B. Silver Co. v. Federal Trade Commission*, 289 Fed. 985 (1923). As one of the circuit judges expressed his view of the issues in this case, "It interests not the whole public, but only those on farms; not all farmers, but only those who are stock-raisers, not all stock-raisers, but only swine breeders, and not all swine breeders but only those with predilections for the Chester type."

A further modification of policy, announced at the same time as that just mentioned, demonstrates even more clearly the tardy recognition by the Commission of the significance of its option to decline to proceed in any case if it deems the interest of the public is not involved. Discussing its power to settle applications for complaints by stipulations with accused parties, the Commission states: "If it were not for the public interest clause it might appear that the statute would be mandatory. It remains to determine what effect the public interest clause has. In the interest of economy and dispatch of business, as well as the desirability of accomplishing the ends of the Commission with as little harm to respondents as possible, all cases should be so settled where they can be *except* where the public interest demands otherwise. But when the very business itself of the proposed respondent is fraudulent, it may well be considered by the Commission that the protection of the public demands that the regular procedure by complaint and order shall prevail. Indeed, there are some cases where that is the only course which would be of any value at all; as for instance the so-called Blue Sky cases and all such where the business itself is inherently fraudulent or where a business of a legitimate nature is conducted in such a fraudulent manner that the Commission is warranted in the belief that no agreement made with the proposed respondent will be kept by him. The rule shall be that all cases shall be settled by stipulation except when the public interest demands otherwise for the reasons set forth above. . . ."

This announcement was coupled with another providing for informal hearings before the issuance of complaints. In practice, these changes of policy and procedure mean that a business concern against whom charges of unfair competition have been made may confer with the Commission and, by pledging itself to discontinue the objectionable method, avoid the defense of public proceedings which might impair its reputation and good-will.<sup>1</sup> This is providing the alleged offense is not of a fraudulent character. It would be fruitless

<sup>1</sup> It should be noted that this modification of policy is, also, a reversion to a previous policy. The Commission by resolution of February 7, 1923, put into effect a similar procedure, which remained in force until October of that year.

to attempt a forecast of the concrete results of these changes, which obviously must depend entirely on the mode in which the Commission now undertakes to exercise its discretion under the public interest clause. But the fundamental significance of this final recognition by the Commission that it possesses a vital discretion in the issuance of complaints, other than in regard to the determination of reasonable indications of a violation of the law, may well be stressed. These announced changes in policy and procedure clearly tend toward the development of greater elasticity and dispatch in the administrative function of the Commission.<sup>1</sup> The importance of this transformation should not be lost sight of in any consideration of the alleged incongruity of an essentially administrative body acting in a judicial capacity.

#### §8. PUBLICITY RULES AND THE ADMINISTRATIVE CHARACTER OF THE COMMISSION

Still another circumstance which has led to criticisms of Federal Trade Commission procedure, some just and some unjust, relates to the publicity methods adopted by the Commission. When a complaint is issued the fact is announced through the daily press in a broadcasted statement setting forth the charges preferred and identifying the respondent. Since June, 1923, these "press releases" have invariably carried the explanation that, while the Commission has reason to believe that an unfair method of competition has been used, "the question whether or not such method has been used is not passed upon by the Commission finally until after respondents have had thirty days in which to answer and the issue has been tried out."<sup>2</sup> The impression conveyed by these public announcements is that the Commission has sat as a grand jury and determined that there was sufficient evidence in the case to warrant the institution of judicial proceedings. But in fact, of course, the Commission neither

<sup>1</sup> See article by Gilbert H. Montague, "Trade Board Will Play A New Rôle in Business," *New York Times*, June 14, 1925.

<sup>2</sup> Prior to June, 1923, no uniform practice prevailed, but usually some such statement appeared in the announcement as that, "The respondents are given thirty days in which to answer, after which the Commission will set a day for further trial of the case."

does, nor ought to, proceed in issuing complaints after the manner of a grand jury bringing criminal indictments. If it did and were itself to constitute the trial court the indictment, in the form of a complaint, might well be equivalent to a verdict of guilty, in the form of an order to cease and desist. The Commission acts under a law that is corrective and not penal. Quite properly, therefore, the issuance of a complaint is made a matter of primary responsibility of the Board of Review, a part of the Legal Division, charged with the prosecuting function. This subordinate agency, composed of five lawyers, acts, of course, in conformity with general lines of policy formulated by the Commission, and its recommendations are acted upon finally by the Commissioners according to their own judgment. But the determination of the adequacy of the evidence to support a complaint in a particular case rests mainly with this branch of the Legal Division. The commissioners do not, in the ordinary course, receive any information concerning the pendency of a case, let alone concerning its parties or subject matter, until it is presented to one of their number, under the rotation scheme, in the form of a specific recommendation of the Board of Review.<sup>1</sup> Though no statistical record is kept, it is unofficially estimated that above ninety percent of the recommendations of the Board of Review have been accepted by the Commission. It is stated, moreover, that of the few recommendations not endorsed the majority have been recommendations that a complaint be not issued. While the action of the commissioners in filing or declining to file a complaint is not a mere formality, therefore, it is evident that they can in the nature of things have little first hand intimate acquaintance with the concrete grounds for taking action in particular cases. The preliminary procedure leading to the issuance of complaints seems designed to enable the commissioners themselves, so far as possible, to reserve judgment upon each case until an actual hearing has been held.

<sup>1</sup> See Annual Report, 1923, p. 4. There is an exception to this general rule in the case of a recommendation by the investigating attorney against the issuance of a complaint. In such case the file goes to a commissioner directly, instead of to the Board of Review. See Annual Report, 1924, p. 22. Formerly it appears to have been the practice to submit even applications for complaint, as they were received, to individual members of the Commission. See Annual Report, 1916, p. 7.

In these circumstances, the public announcement in the press of the issuance of complaints appears to be ill-advised. It subjects a respondent to unfavorable publicity which may and often does prove after hearing to be unmerited. But looking at the procedure solely from the point of view of the Commission as an administrative agency it is equally unfortunate. It emphasizes, one may even say over-emphasizes, the judicial character of the Commission. The proceedings take on the aspect essentially of a trial of a culprit instead of an investigation to determine whether a modification of the business practice in question would be in the public interest. There is a deep and vital difference between these two conceptions of administrative function. In fact, strictly considered the conception of the Federal Trade Commission as a trial tribunal negatives the whole notion of the Commission as an administrative organization.

It is the great misfortune of the Commission that it has encouraged the public and the business community to regard it as a court by its policy of treating complaints as substantial documents of such moment as to justify their wide-spread circulation. For the correlative of this policy is conduct of hearings as criminal trials directed to the determination of the culpability of the particular respondents. And the order of the Commission becomes a sentence. Now in some instances the respondents may be criminals. Frequently, however, they are only unwitting transgressors of the admittedly indefinite standards of fair competition, or they may even be unjustly accused of offenses not committed. But, however the event may prove, in that respect, it is quite beside the point in any consideration of Federal Trade Commission procedure. For the basic and controlling fact remains that the Commission does not act under a penal law. If there is punishment to be meted out, it is not for the Commission to be the assessor. It cannot be too often reiterated that the process of commission regulation is "prophylactic" and not punitive. If misdemeanors under the statutes grow out of trade competition, as they sometimes do, they lie wholly outside and beyond the jurisdiction of the Federal Trade Commission. There are other agencies of government responsible for the execution of penal laws as applied to

trade and industry. They have a quite different function from the Commission, and each should approach its duties in a distinctive manner.

Such being the case, it follows that the complaints filed by the Commission are essentially only the formal device for instituting, in accordance with the provisions of the statute, an inquiry into the fairness under all the circumstances of a given course of business conduct. The complaint has no such status either in fact or in theory as warrants its being sent broadcast to the newspapers at government expense, heralding that the Commission believes the respondent to be violating the law. It is, of course, a matter of public record. But it is one thing to hold the docket of the Commission open to public inspection, and another and quite different thing to announce through an organized publicity service every proceeding initiated by the Commission. It is the order, which follows the hearing in which a presentation of all sides of the question at issue may be made, that the Commission is justified in taking active steps to have published. Lacking any sanctions for the enforcement of its orders and engaged in what is essentially the work of business sanitation the assistance of an informed public opinion in fostering observance of the law cannot be minimized.

This matter of publicity, though it may seem insignificant in itself, really brings to an issue two radically opposite conceptions of the purpose and character of the Commission. This has been demonstrated in the recent controversy within the Commission itself over the amendment of its rules of procedure. In April, 1925, the Commission announced the adoption, by a majority consisting of three members, of a new policy to the effect that, "In the settlement of any matter by stipulation before complaint is issued, no statement in reference thereto shall be made by the Commission for publication. After a complaint is issued, no statement in regard to the case shall be made by the Commission for publication until after the final determination of the case." The manifest purpose of this rule is to facilitate the development of greater toleration of and cooperation with the Commission by business men. A minority of the commissioners

vigorously dissent from this new orientation of policy. "It is true," they declare, "that it is the duty of the Commission to put a stop to unfair methods of competition. That object can only be obtained by 'pitiless publicity' concerning those who are willfully guilty of such methods." But it might be inquired if the attainment of that object also necessitates the employment of "pitiless publicity" against those who are neither willful nor inadvertent violators of the law, as occurred unavoidably under the former publicity policy of the Commission.

It would be imprudent to attempt, however, a detailed assessment of the new rules of procedure in their entirety or an exposition of their definite content and meaning. What may be safely ventured, nevertheless, is that, in the fundamental issue now joined in the debate within the Commission, the statesmanlike point of view is that of the majority. When the issue is resolved into the simple question of whether the Commission shall be administered in the spirit of a crusade against the unfaithful in business or in the spirit of a public confessor and missionary encouraging penitents and seeking converts from the ranks of commercial sinners, there can be little doubt which method will in the long run prove most effective and best serve the common interest. Yet such is in substance the issue lying at the bottom of the current controversy. If the majority of the Commission prevail, no matter how ill-considered and poorly devised may be the specific measures they have adopted or may presently adopt for putting into effect their conception of sound administrative policy, it will surely make the Commission in the long run a more constructive force in the upbuilding of American industry. For the strength and vigor of the industrial and commercial system by which modern wealth is produced and distributed springs from spontaneous enterprise and free competition. Coercive regulation is an anomaly in such a system, and only within minimum limits can it be maintained without undermining the whole organization by attacking the primary motives upon which reliance is placed. Only a system of administrative regulation which permits and encourages business voluntarily to purge itself of abuses and unfair practices inimical to its own sustained prosperity

can in the end accomplish its fundamental purpose. Relentless persecution and pitiless publicity should be reserved for proven malefactors. Investigation, conference, negotiation, and warning should be the most characteristic methods of Federal Trade Commission procedure.

### §9. THE TRADE PRACTICE SUBMITTAL

The prospect of a further and more pronounced development of cooperation between the Commission and business in the elimination of unfair practices suggests reflection upon what has been hitherto accomplished in this direction. While the distinctive rôle of the Commission thus far has been that of a vigorous prosecutor, it has upon occasion experimented with other methods of securing respect for and concrete definition of the laws it is charged to enforce. Most conspicuous has been the work of the Commission in fostering voluntary joint efforts to rid particular lines of trade of wide-spread abuses and irregularities and to secure the formulation of recognized commercial standards. This is the so-called trade practice submittal.<sup>1</sup> Sometimes unfair and pernicious practices come to permeate an entire industry through the inability of individual producers acting singly to resist the outside pressure for the adoption of selling tactics, known and recognized by most producers to be a handicap upon the trade. To deal with such situations effectively and equitably the Commission devised in 1919 a special procedure for which there is no specific statutory authority, but which may probably be sanctioned under the general direction of the Commission to prevent unfair methods of competition. It should be noted, however, that this procedure has been employed not only on the initiative of the Commission but also at the request of the industries affected,<sup>2</sup> thus evincing even more plainly the desire of the Commission to encourage the voluntary elevation of business standards.

<sup>1</sup> Approximately twenty trade practice submittals have been held in the past six years. The industries covered include Book and Writing Paper, Creamery, Rebuilt Typewriter, Celluloid, Package Macaroni, Gold-filled Watch Case, Sheet Music, Band Instrument, and Silver Plated Hollow-Ware.

<sup>2</sup> See Annual Report, 1920, p. 43. The trade practice submittal of Subscription Book Publishers was held at the request of the Subscription Book Publishers Association. See Press Release, July 31, 1924.



The trade practice submittal consists of an informal conference between representatives of the several concerns in an industry, arranged by the Commission and held in the presence of one or more members of the Commission. Questionable practices pertaining to the industry are discussed and the collective opinion of the trade regarding such practices is formulated. The agreement or resolution, reduced to writing, is signed by as many of the participants as concur. No legal obligation is created by these resolutions on the part of any of the concerns represented, subscribing or non-subscribing. Least of all is the Federal Trade Commission which is not formally a party to the deliberations bound by any action taken. At the same time, the Commission has indicated its intention to give considerable weight in any subsequent proceedings involving the subject matter of these submittals to the considered opinions of the trade. In the official announcement of one of the earliest conferences held the statement was made: "It was understood that the judgment of the industry, as expressed, should be for the guidance of the Commission and should be regarded as, *prima facie*, law merchant for this industry."<sup>1</sup> In reporting the more recent trade practice submittals the Commission has shown more caution about committing itself to the views formulated by the conferees. Several submittals have been criticized in detail<sup>2</sup> and others flatly rejected.<sup>3</sup> Nevertheless, when the outcome of the deliberations has been acceptable to the Commission it has, in several instances, supported the voluntary action of the majority members of the industry by instituting formal proceedings against those refusing to conform to the standard practice.<sup>4</sup>

<sup>1</sup> "Trade Practice Submittals," Federal Trade Commission, Washington, 1923, p. 2.

<sup>2</sup> See, for example, reports of the silver plated hollow-ware industry submittal (January 19, 1922) and the gold-mounted knife manufacturers' submittal. (May 2, 1922) "Trade Practice Submittals," *op. cit.*, pp. 40-44; and 44-51, respectively.

<sup>3</sup> The Commission announced its disapproval of the use of the terms "Engraved Effect" and "Embossed Effect" to describe products of the printing industry imitating genuine engraved or embossed work. This trade practice submittal was held on October 28, 1924. Public announcement was made through a press release of January 18, 1925.

<sup>4</sup> The complaint against the *Mountain Grove Creamery . . . Co.*, 6 F. T. C. 426 (1923), illustrates Commission procedure in such cases. Paragraph 5 of the Findings in that proceedings states: "Butter manufacturers competing in the states

The effort, so far as possible, to eliminate improper methods by conference and mutual agreement rather than by the coercive measures of complaint and order has many advantages. It affords an opportunity to enlist the interest and vigilance of the great body of law-observing business concerns in securing a more scrupulous regard for the rights of others in trade competition. It facilitates the prompt adoption of new standards of fair dealing to fit the requirements of changing technical processes. It provides a mechanism for the abolition of minor abuses which might otherwise engage a disproportionate share of the Federal Trade Commission's attention. The chief value of the trade practice submittal, however, lies in the contribution of the special knowledge of men active in industrial and commercial affairs in different lines of trade to the formulation of specific rules applicable to particular business spheres, embodying the general principles and standards worked out by the Federal Trade Commission and the courts. The latter are necessarily and properly guided by legal traditions and precedents. But it is highly desirable that the Federal Trade Commission through close and frequent contact with those familiar with practical conditions should be influenced by the teachings of common experience. The extension of trade practice submittals is one way in which this cooperation may be fostered.

of Arkansas, Oklahoma and Texas assembled at the invitation of the Federal Trade Commission at Dallas, Texas, on April 2, 1920, and there in open meeting, presided over by a duly authorized representative of the Commission, did by means of resolution define and denounce said method of competition which in the experience of the industry had proven to result in fraud on the public. . . . August 1, 1920, was named in the same resolution as the day upon which the practice or method so denounced was to entirely cease and which on said day did practically cease; among the purposes understood by respondent to be intended to be accomplished by the institution and adoption of such 'Trade Practice Submittal' was the obviation of a multiplicity of formal proceedings due to the voluntary and simultaneous action of the industry in eliminating the method or practice so defined and denounced. Said Trade Practice Submittal is stipulated to be and is part of the facts herein. Respondent continued the practice charged in the complaint . . . after said August 1, 1920, and until January, 1922." The Commission concluded that the practice of the respondent in dressing and packing butter in odd-weight units resembling butter cartons of the standard sizes, "under the conditions and circumstances described in the foregoing findings," was an unfair method of competition.

### §10. THE CONTRIBUTION OF VOLUNTARY COOPERATION AND AUTONOMOUS CONTROL TO IMPROVEMENT OF BUSINESS STANDARDS

Other indications of cooperation from business are found in the increasing number of applications for complaints received from trade associations and similar organizations interested in ridding business of objectionable practices. While the identity of applicants for complaints is never revealed, yet sufficient is known of the activity in this respect of organizations like the Unfair Competition Bureau of the National Varnish Manufacturers' Association and the Paint Manufacturers' Association to warrant the conclusion that so far as methods of competition inherently vicious and unfair are concerned there is an increasing tendency for organized business to cooperate with the Federal Trade Commission.<sup>1</sup> One of the commissioners has stated that ninety percent of the complaints originate in applications from business men and business organizations, but this figure includes a large proportion of competitors having a direct and substantial personal interest in the cessation of the practices complained of.

Still more significant of the growing interest and activity of business leaders in ridding the commercial world of unfair practices is the organization of cooperative agencies for investigating and prosecuting false advertising and the myriad forms of commercial fraud. The National Association of Credit Men has long conducted an active campaign against fraudulent business enterprises, which is a protection not only to credit grantors but also to competitors and everyone with whom they transact business.<sup>2</sup> Recently this association has announced its intention to carry on this work even more intensively and vigorously than in the past, and has appropriated a large fund for that purpose.<sup>3</sup>

The truth in advertising movement initiated by the

<sup>1</sup> See Report of the Unfair Competition Bureau to the National Varnish Manufacturers' Association and the Paint Manufacturers' Association of the United States. Philadelphia, October, 1924.

<sup>2</sup> See "Commerce and The Credit Crook," National Association of Credit Men, New York, 1924, and the files of the "Credit Monthly," published regularly by the Association since 1898.

<sup>3</sup> New York Times, June 11, 1925. A million dollar fund is reported to have been raised and placed at the disposal of the association.

Associated Advertising Clubs of the World and affiliated Better Business Bureaus bespeaks a wide and growing sense of responsibility among business men for the elimination of deceptive methods of merchandizing. Since the organization of the National Vigilance Committee by the Associated Clubs in 1911 to coordinate the activities of the local bureaus, this work has been expanded and solidified into a nation-wide campaign for the protection of honest business against the insidious competition which depends on deceit and misrepresentation. Certain types of commercial crooks have hardly less to fear now from these voluntary organizations than from the Federal Trade Commission. They are unrestrained by the division of state and national jurisdiction, and where publicity is not an adequate weapon they can bring to bear the pressure of state authority under statutes against misrepresentation and fraud of which they have been largely instrumental in securing the passage. Representing advertisers, publishers, bankers, manufacturers, and merchants, the truth in advertising movement expresses the confidence of an important cross-section of the business community in the efficacy of autonomous control for the prevention of unfair methods of competition. Among publishers separately there has been a noteworthy advance in recent years in the development of standards of dependability for acceptable advertising. Several magazines of large circulation definitely guarantee the truth of their advertising, and maintain testing laboratories with trained technical staffs for verifying the statements and claims of advertisers. The Periodical Publishers' Association of America has formulated certain Principles of Censorship, "which within the limits of human vigilance govern our acceptance of advertising accounts and copy."<sup>1</sup> These principles have to do, among other things, with the truthfulness and educational value of the advertising, the reliability of the advertiser, and the attitude expressed towards competitors, condemning disparagement.

The transformation going on in the commercial world from cut-throat warfare, with its subordination of ethical to profit considerations, towards a more chivalrous competition may have been aided by the administrative regulation of business

<sup>1</sup> Bulletin of Periodical Publishers' Assn. of America. New York City.

practices. But that it is fundamentally a spontaneous conversion is indicated by the significant development latterly of these voluntary organizations which would purge trade competition of corrupt and unfair methods. This is not to depreciate the accomplishments of government regulation as represented in the record of the Federal Trade Commission. In a negative way they have undoubtedly been considerable, and the gesture of compulsion will still continue for a long while to be an indispensable feature of any effective program for maintaining fair competition and open markets. But it is to emphasize that the real basis for hope of the preservation of the competitive system of business enterprise lies in its own power of self-regulation. No authoritative control of unfair business practices, however wisely conceived or efficiently administered, can ever take the place of a vigilant and virulent insistence upon fair play and straightforward business methods by those who participate in the game. Only through the further development of the autonomous control of the conditions of free and fair competition can the objects for which the Federal Trade Commission was established be finally achieved.

## **APPENDICES**

**APPENDIX A**  
**SUMMARY RECORD OF FEDERAL TRADE COMMISSION**  
**PROCEEDINGS BY FISCAL YEARS ENDING**  
**JUNE 30, 1915-1924**

This statistical summary must be examined with the following limitations in mind:

(1) Any classification of unfair methods of competition is necessarily arbitrary. For example, the heading "Misrepresentation as to character of product" might be sub-divided into such groups as false advertising, misbranding, false packaging, etc. It is believed, however, that the present classification is sufficiently comprehensive for the purpose of analyzing the character and direction of Federal Trade Commission activity, which was the object of its compilation.

(2) The distribution of cases under the various headings must also frequently be arbitrary. The distinction between misrepresentation of price and misrepresentation of character of product, for example, is sometimes difficult to make. Moreover, in many instances several diverse business methods have been the basis of the complaints and orders. In all such cases the classification was determined by the relative emphasis apparently given to the respective charges in the complaint or order.

(3) Complaints and orders are classified separately, it will be observed. As a result of the fact that in many instances the major charge in the complaint was either disproved, abandoned or relegated to a minor place in the findings of fact, the number of orders issued against a given practice bears relatively slight relation to the number of complaints. This also explains some curious anomalies in the table, e. g., the appearance of an order issuing in 1919 against false claim to use or endorsement, although no previous complaint against this particular practice is indicated.

(4) The yearly totals of orders and dismissals do not in every instance correspond with those given in the Trade Commission's Annual Report, 1924, p. 62. The only explanation which suggests itself is that while the date of each order in this compilation is that of the original order the commission has reclassified cases in which an order was subsequently suspended, modified or reversed. Any attempt to indicate such changes in this table would serve no useful purpose.

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SUMMARY RECORD OF FEDERAL TRADE COMMISSION PROCEEDINGS, 1915-1924, BY FISCAL YEARS ENDING JUNE 30

	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.
	1916							1917						
Misrepresentation as to:														
Character of product.....	3	..	..	..	..	..	..	2	1	..	..	..	..	..
Use or endorsement.....	..	..	..	..	..	..	..	..	1	..	..	..	..	..
Trade status.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Place of origin.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Price.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Corporate securities.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, misrepresentation..	3	..	..	..	..	..	..	2	1	..	..	..	..	..
Trade-mark simulation, etc....	..	..	..	..	..	..	..	..	1	..	..	..	..	..
Bogus independents.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Commercial bribery.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Subsidies to salesmen.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Lottery sales methods.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Disparagement.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Harassing tactics:														
Not otherwise classified....	1	..	..	..	..	..	..	..	..	..	..	..	..	..
Espionage.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Writing for catalogues.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Enticement of employees....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Inducing breach of contract	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Bidding up supplies.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Threatening litigation.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, harassing tactics..	1	..	..	..	..	..	..	1	..	..	..	..	..	..
Resale price maintenance.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Price guarantee.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Selling below cost.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Refusal to deal.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Clayton Act violation:														
Tying contracts.....	1	..	..	..	..	..	..	3	1	..	..	..	..	..
Exclusive dealing.....	..	..	..	..	..	..	..	2	..	..	..	..	..	..
Price discrimination.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Control of competitors.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Interlocking directorates....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, Clayton Act.....	1	..	..	..	..	..	..	5	1	..	..	..	..	..
Conspiracy:														
to maintain trade channels..	..	..	..	..	..	..	..	1	..	..	..	..	..	..
to fix prices.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
to coerce for other objects..	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, conspiracy.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Miscellaneous.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Totals.....	5	..	..	..	..	..	..	9	3	1	..	..	..	..



SUMMARY RECORD OF FEDERAL TRADE COMMISSION PROCEEDINGS,  
1915-1924, BY FISCAL YEARS ENDING JUNE 30—(Continued)

	Complaints	Orders to Denist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.	Complaints	Orders to Denist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.
	1918							1919						
Misrepresentation as to:														
Character of product.....	10	4	..	..	..	..	..	11	5	3	..	..	..	..
Use or endorsement.....	..	..	..	..	..	..	..	1	1	..	..	..	..	..
Trade status.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Place of origin.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Price.....	2	1	..	..	..	..	..	1	2	..	1	..	..	..
Corporate securities.....	..	..	..	..	..	..	..	2	..	..	..	..	..	..
Total, misrepresentation.....	12	5	..	..	..	..	..	16	9	3	1	..	..	..
Trade-mark simulation, etc....	1	1	..	..	..	..	..	8	2	..	..	..	..	..
Bogus independents.....	1	..	..	..	..	..	..	1	1	..	..	..	..	..
Commercial bribery.....	54	39	2	..	..	..	..	47	34	1	..	..	..	..
Subsidies to salesmen.....	1	2	..	..	..	..	..	4	..	..	..	..	..	..
Lottery sales methods.....	23	15	1	..	..	..	..	..	3	4	..	..	..	..
Disparagement.....	7	1	..	..	..	..	..	4	1	1	..	..	..	..
Harassing tactics:														
Not otherwise classified.....	2	..	..	..	..	..	..	..	..	..	..	..	..	..
Espionage.....	..	..	..	..	..	..	..	1	1	..	..	..	..	..
Writing for catalogues.....	..	1	..	..	..	..	..	2	2	..	..	..	..	..
Enticement of employees.....	..	1	..	..	..	..	..	1	..	..	..	..	..	..
Inducing breach of contract	6	..	..	..	..	..	..	..	2	..	..	..	..	..
Bidding up supplies.....	3	..	..	..	..	..	..	..	1	..	..	..	..	..
Threatening litigation.....	4	2	..	..	..	..	..	5	2	1	..	..	..	..
Total, harassing tactics.....	14	4	..	..	..	..	..	9	8	1	..	..	..	..
Resale price maintenance.....	19	1	1	..	..	..	..	31	9	1	..	..	..	..
Price guarantee.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Selling below cost.....	4	..	..	..	..	..	..	..	1	1	..	1	..	..
Refusal to deal.....	..	..	..	..	..	..	..	1	1	..	..	..	..	..
Clayton Act violation:														
Tying contracts.....	..	..	1	..	..	..	..	4	1	..	..	1	..	..
Exclusive dealing.....	6	..	..	..	..	..	..	2	1	..	..	..	..	..
Price discrimination.....	1	..	2	..	..	..	..	2	..	..	..	..	..	..
Control of competitors.....	1	..	..	..	..	..	..	1	..	..	..	..	..	..
Interlocking directorates.....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, Clayton Act.....	8	..	3	..	..	..	..	9	2	..	..	1	..	..
Conspiracy:														
to maintain trade channels..	2	1	..	..	..	..	..	3	1	..	..	..	..	..
to fix prices.....	4	3	..	..	..	..	..	..	1	1	..	..	..	..
to coerce for other objects..	2	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, conspiracy.....	8	4	..	..	..	..	..	3	2	1	..	..	..	..
Miscellaneous.....	2	..	..	..	..	..	..	1	1	..	..	..	..	..
Totals.....	154	72	7	..	..	..	..	135	74	13	1	2	..	..

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SUMMARY RECORD OF FEDERAL TRADE COMMISSION PROCEEDINGS,  
1915-1924, BY FISCAL YEARS ENDING JUNE 30—(Continued)

	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.
	1920							1921						
Misrepresentation as to:														
Character of product.....	83	31	1	..	..	..	..	31	27	9	..	1	..	..
Use or endorsement.....	5	1	1	..	..	..	..	8	6	..	..	..	..	..
Trade status.....	2	..	..	..	..	..	..	3	3	..	..	..	..	..
Place of origin.....	5	1	..	..	..	..	..	2	3	1	..	..	..	..
Price.....	11	2	1	..	..	..	..	18	6	2	..	..	..	..
Corporate securities.....	5	1	..	..	..	..	..	8	2	2	..	..	..	..
Total, misrepresentation.....	111	36	3	..	..	..	..	67	45	14	..	1	..	..
Trade-mark simulation, etc....	12	7	2	..	..	..	..	17	4	2	..	..	..	..
Bogus independents.....	..	1	1	..	..	..	..	1	..	..	..	..	..	..
Commercial bribery.....	42	33	5	..	1	..	..	63	46	1	..	..	..	..
Subsidies to salesmen.....	8	4	..	..	..	..	..	1	1	..	..	..	..	..
Lottery sales methods.....	1	..	..	..	..	..	..	1	1	..	..	..	..	..
Disparagement.....	5	..	1	..	..	..	..	1	3	1	..	..	..	..
Harassing tactics:														
Not otherwise classified....	..	..	1	..	..	..	..	..	..	..	..	..	..	..
Espionage.....	3	..	..	..	..	..	..	..	1	..	..	..	..	..
Writing for catalogues.....	..	..	..	..	..	..	..	1	..	..	..	..	..	..
Enticement of employees....	2	..	1	..	..	..	..	..	..	..	..	..	..	..
Inducing breach of contract	..	..	3	..	..	..	..	..	..	..	..	..	..	..
Bidding up supplies.....	..	1	1	..	..	..	..	1	..	..	..	..	..	..
Threatening litigation.....	2	1	2	..	..	..	..	2	2	2	..	..	..	..
Total, harassing tactics....	7	1	8	..	..	..	..	4	3	2	..	..	..	..
Resale price maintenance.....	16	1	9	..	1	..	..	1	1	..	..	..	..	..
Price guarantee.....	10	..	1	..	..	..	..	..	..	..	..	..	..	..
Selling below cost.....	2	..	3	..	..	..	..	..	..	..	..	..	..	..
Refusal to deal.....	1	..	..	..	..	..	..	..	1	..	..	..	..	..
Clayton Act violation:														
Tying contracts.....	41	26	1	..	..	1	10	10	8	..	8	..	..	
Exclusive dealing.....	29	1	6	..	..	..	3	..	8	..	2	..	..	
Price discrimination.....	2	1	1	..	..	..	2	..	1	..	..	..	..	
Control of competitors.....	13	..	1	..	..	..	4	1	..	..	..	..	..	
Interlocking directorates....	..	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, Clayton Act.....	85	28	9	..	..	1	19	11	17	..	10	..	..	
Conspiracy:														
to maintain trade channels..	4	1	..	..	..	..	1	2	..	1	..	..	..	
to fix prices.....	1	..	..	..	..	..	1	1	..	..	..	..	..	
to coerce for other objects..	2	..	1	..	..	..	1	..	..	..	..	..	..	
Total, conspiracy.....	7	1	1	..	..	..	3	3	..	1	..	..	..	
Miscellaneous.....	..	..	2	..	..	..	..	..	..	..	..	..	..	..
Totals.....	308	111	44	..	2	1	177	119	37	1	11	..	..	

SUMMARY RECORD OF FEDERAL TRADE COMMISSION PROCEEDINGS,  
1915-1924, BY FISCAL YEARS ENDING JUNE 30—(Continued)

	1922						1923						
	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.
Misrepresentation as to:													
Character of product.....	21	12	5	1	..	1	28	45	6	2	..	..	..
Use or endorsement.....	6	3	2	..	..	..	3	1	3	..	..	..	..
Trade status.....	1	1	..	..	..	..	15	3	..	..	..	..	..
Place of origin.....	6	2	1	..	..	..	3	2	..	..	..	..	..
Price.....	18	27	8	..	..	..	4	5	..	..	..	..	..
Corporate securities.....	13	1	5	..	..	..	12	..	4	..	..	..	..
Total, misrepresentation.....	65	46	21	1	..	1	65	65	13	2	..	..	..
Trade-mark simulation, etc....	7	15	2	..	..	..	11	2	2	1	..	..	..
Bogus independents.....	..	..	2	..	..	..	..	..	..	..	..	..	..
Commercial bribery.....	14	21	15	..	2	..	2	1	9	..	..	..	..
Subsidies to salesmen.....	..	..	6	..	1	..	..	1	1	..	..	..	..
Lottery sales methods.....	1	..	..	..	..	..	..	1	..	..	..	..	..
Disparagement.....	4	..	..	..	..	..	1	2	1	..	..	..	..
Harassing tactics:													
Not otherwise classified.....	..	..	1	..	..	..	..	..	..	..	..	..	..
Espionage.....	..	..	1	..	..	..	..	..	1	..	..	..	..
Writing for catalogues.....	2	..	..	..	..	..	..	..	..	..	..	..	..
Enticement of employees.....	..	..	..	..	..	..	..	..	..	..	..	..	..
Inducing breach of contract	..	1	..	..	..	..	2	1	..	..	..	..	..
Bidding up supplies.....	..	..	1	..	..	..	2	..	..	..	..	..	..
Threatening litigation.....	2	..	..	..	..	..	2	..	1	..	..	..	..
Total, harassing tactics.....	4	1	3	..	..	..	6	1	2	..	..	..	..
Resale price maintenance.....	6	1	1	..	..	1	37	1	41	1	..	..	..
Price guarantee.....	..	..	..	..	..	..	1	..	2	..	..	..	..
Selling below cost.....	1	..	1	..	..	..	1	..	1	..	..	..	..
Refusal to deal.....	..	..	..	..	1	..	..	..	..	..	..	..	..
Clayton Act violation:													
Tying contracts.....	..	..	2	..	1	..	..	..	7	..	3	..	4
Exclusive dealing.....	1	..	16	..	..	..	2	..	4	..	..	..	1
Price discrimination.....	2	3	..	..	..	..	1	..	..	..	1	..	..
Control of competitors.....	2	1	1	1	..	..	5	3	3	..	..	..	..
Interlocking directorates.....	..	..	..	..	..	..	..	..	..	..	..	..	..
Total, Clayton Act.....	5	4	19	1	1	..	8	3	14	..	4	..	5
Conspiracy:													
to maintain trade channels..	..	2	2	2	..	..	4	1	..	1	..	..	..
to fix prices.....	2	..	..	..	..	..	4	1	1	..	..	..	..
to coerce for other objects..	2	1	3	..	..	..	3	..	..	..	..	..	..
Total, conspiracy.....	4	3	5	2	..	..	11	..	1	1	..	..	..
Miscellaneous.....	..	..	..	..	..	..	1	..	..	..	..	..	..
Totals.....	111	91	75	4	5	2	144	78	37	5	4	..	5

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SUMMARY RECORD OF FEDERAL TRADE COMMISSION PROCEEDINGS,  
1915-1924, BY FISCAL YEARS ENDING JUNE 30—(Continued)

	Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.	Summary						
								Complaints	Orders to Desist	Dismissals	Sustained Circuit Ct.	Reversed Circuit Ct.	Sustained Sup. Ct.	Reversed Sup. Ct.
1924														
Misrepresentation as to:														
Character of product.....	43	39	4	1	..	..	..	235	165	29	4	1	1	..
Use or endorsement.....	6	5	..	..	..	..	..	28	17	6	..	..	..	..
Trade status.....	17	7	2	..	..	..	..	36	15	2	..	..	..	..
Place of origin.....	3	5	..	..	..	..	..	20	13	2	..	..	..	..
Price.....	3	4	..	..	..	..	..	57	47	11	1	..	..	..
Corporate securities.....	1	4	2	..	..	..	..	41	15	13	..	..	..	..
<b>Total, misrepresentation.</b>	<b>78</b>	<b>64</b>	<b>8</b>	<b>1</b>	..	..	..	<b>417</b>	<b>272</b>	<b>63</b>	<b>5</b>	<b>1</b>	<b>1</b>	..
Trade-mark simulation, etc....	10	7	2	..	..	..	..	66	38	10	1	..	..	..
Bogus independents.....	..	..	..	..	..	..	..	3	1	2	..	..	..	..
Commercial bribery.....	5	1	..	..	..	..	..	228	175	33	..	3	..	..
Subsidies to salesmen.....	..	..	..	..	..	..	..	15	7	7	..	1	..	..
Lottery sales methods.....	4	1	4	..	..	..	..	29	21	9	..	..	..	..
Disparagement.....	1	1	..	..	1	..	..	24	8	4	..	1	..	..
Harassing tactics:														
Not otherwise classified.....	..	1	..	..	..	..	..	3	1	2	..	..	..	..
Espionage.....	..	..	..	..	..	..	..	4	2	2	..	..	..	..
Writing for catalogues.....	..	..	..	..	..	..	..	5	3	..	..	..	..	..
Enticement of employees.....	1	..	..	..	..	..	..	5	1	1	..	..	..	..
Inducing breach of contract.....	..	1	..	..	..	..	..	8	5	3	..	..	..	..
Bidding up supplies.....	..	..	..	..	..	..	..	5	1	2	..	..	..	..
Threatening litigation.....	1	1	..	..	..	..	..	18	8	6	..	..	..	..
<b>Total, harassing tactics.</b>	<b>2</b>	<b>3</b>	..	..	..	..	..	<b>48</b>	<b>21</b>	<b>16</b>	..	..	..	..
Resale price maintenance.....	22	4	8	..	..	..	..	132	18	61	1	1	1	..
Price guarantee.....	..	..	1	..	..	..	..	12	..	4	..	..	..	..
Selling below cost.....	..	..	..	..	..	..	..	8	1	6	..	1	..	..
Refusal to deal.....	..	..	..	..	..	1	..	2	2	..	..	1	..	1
Clayton Act violation:														
Tying contracts.....	..	..	..	..	..	..	..	59	38	19	..	13	..	5
Exclusive dealing.....	2	1	7	..	1	..	..	45	3	41	..	3	..	1
Price discrimination.....	4	2	2	..	2	..	..	16	6	6	..	3	..	..
Control of competitors.....	1	..	..	..	..	..	..	27	5	5	1	..	..	..
Interlocking directorates.....	2	..	..	..	..	..	..	2	..	..	..	..	..	..
<b>Total, Clayton Act.....</b>	<b>9</b>	<b>3</b>	<b>9</b>	..	<b>3</b>	..	..	<b>149</b>	<b>52</b>	<b>71</b>	<b>1</b>	<b>19</b>	..	..
Conspiracy:														
to maintain trade channels..	9	1	..	..	..	..	..	24	9	2	4	..	..	..
to fix prices.....	11	4	..	..	..	..	..	21	10	2	..	..	..	..
to coerce for other objects..	2	3	2	..	..	..	..	12	4	6	..	..	..	..
<b>Total, conspiracy.....</b>	<b>22</b>	<b>8</b>	<b>2</b>	..	..	..	..	<b>57</b>	<b>23</b>	<b>10</b>	<b>4</b>	..	..	..
Miscellaneous.....	1	..	2	..	..	..	..	5	1	4	..	..	..	..
<b>Totals.....</b>	<b>154</b>	<b>92</b>	<b>36</b>	<b>1</b>	<b>4</b>	..	<b>1</b>	<b>1,197</b>	<b>640</b>	<b>300</b>	<b>12</b>	<b>28</b>	<b>2</b>	<b>7</b>

## APPENDIX B

### DOCUMENTS, ETC., ISSUED BY THE FEDERAL TRADE COMMISSION

#### ACCOUNTING SYSTEMS

Fundamentals of a Cost System for Manufacturers, Washington, D.C., 1916, 31pp.

A System of Accounts for Retail Merchants, Washington, D.C., 1916, 19pp. Reprinted 1920.

#### BRIBERY

Special Report on Commercial Bribery, 65th Congress, 2nd Session, House Doc. No. 1107, Washington, D.C., 1918, 3pp.

Commercial Bribery, Special Report Dealing with the Subject of Commercial Bribery, 66th Congress, 2nd Session, Senate Doc. No. 258, Washington, D.C., 1920, 7pp.

#### CALCIUM ARSENATE

Report on the Calcium Arsenate Industry, Washington, D.C., 1923, 21pp.

#### COAL

Anthracite and Bituminous Coal, Report and Recommendations on the Anthracite and Bituminous Coal Situation and the Relation of Rail and Water Transportation to the Present Fuel Problem, 65th Congress, 1st Session, Senate Doc. No. 50, Washington, D.C., 1917, 420pp.

Bituminous Coal—Quarterly Reports, Revised costs, Suspended June, 1920, Washington, D.C., 1920.

Cost Reports, Coal, 7 vol., Washington, D.C., 1919–1921.

No. 1. Pennsylvania—Bituminous, 1919.

No. 2. Pennsylvania—Anthracite, 1919.

No. 3. Illinois—Bituminous, 1919.

No. 4. Alabama, Tennessee and Kentucky—Bituminous, 1920.

No. 5. Ohio, Indiana and Michigan—Bituminous, 1920.

No. 6. Maryland, West Virginia and Virginia—Bituminous, 1920.

No. 7. Trans-Mississippi States—Bituminous, 1921.

Preliminary Report on Investment and Profit in Soft-Coal Mining, Washington, D.C., 1922, 222pp.

Premium Prices of Anthracite, Washington, D.C., 1925.

#### COPPER

Cost Reports, Copper, Washington, D.C., 1919, 26pp.

#### COTTON

Report on Combed Cotton Yarns, Washington, D.C., 1921, 94pp.

Preliminary Report on the Cotton Trade, Washington, D.C., 1923, 28pp.

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The Cotton Trade, 68th Congress, 1st Session, Senate Doc. No. 100, 2 Parts, Washington, D.C., 1924.

Cotton Merchandising Practices, 68th Congress, 2nd Session, Senate Doc. No. 194, Washington, D.C., 1925, 38pp.

Empire Cotton Growing Corporation, Development, Method and Activities of Empire Cotton Corporation, a British Firm, Washington, D.C., 1925, 30pp.

### DECISIONS

Federal Trade Commission Decisions, Findings and Orders of the Federal Trade Commission, 6 vol., Washington, D.C., 1920-1925.

### FARM IMPLEMENTS

Report on the Causes of High Prices of Farm Implements, Washington, D.C., 1920, 713pp.

### FEEDS

Report on Commercial Feeds, Washington, D.C., 1921, 206pp.

Summary of Report on Commercial Feeds, Washington, D.C., 1921, 15pp.

### FERTILIZER INDUSTRY

Report on the Fertilizer Industry, Washington, D.C., 1916, 269pp.

Report on the Fertilizer Industry, Washington, D.C., 1923, 87pp.

### FLAGS

Prices of American Flags, 65th Congress, 1st Session, Senate Doc. No. 82, Washington, D.C., 1917, 6pp.

### FOOD

Report on Bakery Business in the United States. Report of the Bakery Section of Food Administration, Published by the United States Food Administration, Washington, D.C., 1917, 23pp.

Report on Beet Sugar Industry in the United States, Washington, D.C., 1917, 164pp.

Food Investigation, Report on Canned Foods. General Report and Canned Vegetables and Fruits, Washington, D.C., 1918, 103pp.

Food Investigation, Report on Flour Milling and Jobbing, Washington, D.C., 1918, 27pp.

Food Investigation, Summary of the Report on the Meat Packing Industry, Washington, D.C., 1918, 51pp.

Food Investigation, Report on the Meat Packing Industry, 6 parts, Washington, D.C., 1918-1920.

Part 1 and Summary. Extent and Growth of Power of the Five Packers in Meat and other Industries, 1919.

Part 2. Evidence of Combination among Packers, 1918.

Part 3. Methods of the Five Packers in Controlling the Meat Packing Industry, 1919.

Part 4. The Five Larger Packers in Produce and Grocery Foods, 1920.

Part 5. Profits of the Packers, 1920.

Part 6. Cost of Growing Beef. Cost of Fattening Cattle. Cost of Marketing Livestock, 1920.

Maximum Profit Limitation on Meat Packing Industry. Report of the Results of a Special Investigation of the Reasonableness of the Maximum Profit Limitations Fixed on the Meat Packing Industry by the Food Administration, 66th Congress, 1st Session, Senate Doc. No. 110, Washington, D.C., 1919, 179pp.

Food Investigation, Report on Canned Foods. Canned Salmon, Washington, D.C., 1919, 83pp.

Report on Sugar Supply and Prices, November, 1920, Washington, D.C., 1920, 205pp.

Report on Southern Livestock Prices, 66th Congress, 2nd Session, Senate Doc. No. 209, Washington, D.C., 1920.

Food Investigation, Report on Private Car Lines, Washington, D.C., 1920, 271pp.

Report on Commercial Wheat Flour Milling, Washington, D.C., 1920, 118pp.

Food Investigation, Report on Wholesale Marketing of Food, Washington, D.C., 1920, 268pp.

Report on the Grain Trade, 6 vol., Washington, D.C., 1920-1925.

Vol. I. Country Grain Marketing, 1920.

Vol. II. Terminal Grain Markets and Exchanges, 1920.

Vol. III. Terminal Grain Marketing, 1922.

Vol. IV. Middlemen's Profits and Margins, 1924.

Vol. V. Future Trading Operations in Grain, 1920.

Vol. VI. Prices of Cash Grain and Grain Futures, 1925.

Report on Wheat Prices for the 1920 Crops, Washington, D.C., 1921, 91pp.

Summary of Report on Milk and Milk Products, 1914-1918, Washington, D.C., 1921, 19pp.

Report on Milk and Milk Products, 1914-1918, Washington, D.C., 1921, 234pp.

Food Investigation, Report on Canned Foods, 1918: Corn, Peas, String Beans, Tomatoes and Salmon, Washington, D.C., 1922, 86pp.

Report on Methods and Operations of Grain Exporters, 2 vol., Washington, D.C., 1922-1923.

Vol. I. Interrelations and Profits, 1922.

Vol. II. Speculation, Competition, and Prices, 1923.

Report Concerning the Present Status of the Consent Decree in the Case of the United States vs. Swift and Company, et al., entered in the Supreme Court of the District of Columbia, February 27, 1920, 68 Congress, 2nd Session, Senate Doc. No. 219, Washington, D.C., 1925.

#### FOREIGN TRADE

Schedule on Foreign Trade Conditions; Inquiries for Publicists, Economists, Lawyers, Engineers, etc., Washington, D.C., 1915.

Report on Cooperation in American Export Trade, Part I, Summary and Report. Part II, Exhibits, Washington, D.C., 1916.

Report on Trade and Tariffs in Brazil, Uruguay, Argentina, Chile, Bolivia, and Peru, Washington, D.C., 1916, 246pp.

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Report on Cooperation in Foreign Countries, Washington, D.C., 1925, 202pp.

Foreign Trade Series, Discussion of Practices and Procedure under Export Trade Act, Washington, D.C., 1919, 13pp.

### HOUSE FURNISHINGS

Report on House Furnishings Industries, 3 vol., Washington, D.C., 1923-1925.

Vol. I. House Furniture.

Vol. II. Household Stoves.

Vol. III. Kitchen Furnishings and Domestic Appliances.

### LEATHER INDUSTRIES

Report on Leather and Shoe Industries, Washington, D.C., 1919, 108pp.

Summary of Report on Shoe and Leather Costs and Prices, Washington, D.C., 1921, 15pp.

### LUMBER

Report on Lumber Manufacturers' Trade Associations, Washington, D.C., 1922, 150pp.

Report on War Time Costs and Profits of Southern Pine Lumber Companies, Washington, D.C., 1922, 94pp.

Report on Northern Hemlock and Hardwood Manufacturers' Association, Washington, D.C., 1923, 52pp.

Report on Western Red Cedar Association, Lifetime Post Association, Western Red Cedarmen's Information Bureau, Washington, D.C., 1923, 22pp.

### MISCELLANEOUS

Annual Reports for the Fiscal Years Ending June 30, 1915-1924 inclusive, Washington, D.C., 1915-1924.

Rules of Practice before the Commission. Adopted June 17, 1915, Washington, D.C., 1915, 8pp. Revised edition with amendments to November 19, 1920, Washington, D.C., 1920, 8pp. Revised edition with amendments to May 20, 1921, Washington, D.C., 1921, 11pp. Revised edition with amendments to September 29, 1922, Washington, D.C., 1922, 11pp. Revised edition with amendments to March 12, 1923, Washington, D.C., 1923, 11pp.

Conference Rulings Bulletin, Washington, D.C., 1916. Republished in Federal Trade Commission Decisions, Vol. I, pp. 540-561.

Helpful Activities to Strengthen American Business, Washington, D.C., 1916, 4pp.

Places in the United States having in 1910, 2,500 Inhabitants or More, Washington, D.C., 1919, 10pp.

Acts from which the Commission Derives its Powers with Annotations. Decisions of the Courts on Petitions to Review and Rules of Practice before the Commission, Washington, D.C., 1920, 120pp.

Trade Practice Submittals, 1919-1923, Multigraphed.

Report on the Uses of the Upper Columbia River, Washington, D.C., 1924. Revised edition, 1925.



**PAPER**

- Book-Paper Industry. Final Report of the Findings of Fact, together with Conclusions and Recommendations with Reference to the Book-paper Industry, Washington, D.C., 1917, 125pp.
- Report on the Newsprint Paper Industry, Washington, D.C., 1917, 162pp.
- Wall Paper Review, Monthly, Multigraphed, Discontinued May, 1921, Washington, D.C., 1919-1921.
- Statistical Summary of the Paper and Pulp Industry, Monthly, Multigraphed, Discontinued 1923, Washington, D.C., 1919-1923.
- Newsprint Review, Monthly, Multigraphed, Discontinued December, 1923, Washington, D.C., 1919-1923.

**PATENTS**

- Extracts from the Trading with the Enemy Act and Executive Order of October 12, 1917, and Instructions, Rules and Forms Concerning Patents, Trade Marks, Prints, Labels, Designs and Copyrights, Washington, D.C., 1918, 22pp.

**PETROLEUM**

- Investigation of the Price of Gasoline, A Preliminary Report Relative to an Investigation of Gasoline Price, Washington, D.C., 1916, 15pp.
- Report on Pipe-Line Transportation of Petroleum, Washington, D.C., 1916, 467pp.
- Report on the Price of Gasoline in 1915, Washington, D.C., 1917, 224pp.
- Advance in the Price of Petroleum Products, 66th Congress, 2nd Session, House Doc. No. 801, Washington, D.C., 1920, 57pp.
- Report on the Pacific Coast Petroleum Industry, 2 vol., Washington, D.C., 1921-1922.
  - Vol. I. Production, Ownership, and Profits, 1921.
  - Vol. II. Prices and Competitive Conditions, 1922.
- Report on the Petroleum Industry of Wyoming, Washington, D.C., 1921, 54pp.
- Report on the Petroleum Trade in Wyoming and Montana, Washington, D.C., 1922, 4pp.
- Report on Foreign Ownership in the Petroleum Industry, Washington, D.C., 1923, 152pp.

**PROFITEERING**

- Profiteering, Report Containing all Facts, Figures, Data or Information now in Possession of the Federal Trade Commission Relative to Profiteering, 65th Congress, 2nd Session, Senate Doc. 248, Washington, D.C., 1918, 20pp.

**RADIO INDUSTRY**

- Report on the Radio Industry, Washington, D.C., 1924, 347pp.

**RAG INDUSTRY**

- Report on the Woolen Rag Trade, Washington, D.C., 1920, 90pp.

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### STEEL INDUSTRY

Applications, Answers and Statements Concerning the so-called Pittsburgh Basing Point for Steel, Washington, D.C., 1919, 191pp. Supplement, 1919, 14pp.

Report on War Time Profits and Costs of the Steel Industry, Washington, D.C., 1925, 138pp.

### TAXATION

Taxation and Tax-Exempt Income, Report on Taxation and Tax-Exempt Income in Partial Response to Senate Resolution No. 451, 67th Congress, 4th Session, 68th Congress, 1st Session, Senate Doc. No. 148, Washington, D.C., 1924, 144pp.

### TOBACCO

Report on the Tobacco Industry, Washington, D.C., 1921, 162pp.

Prices of Tobacco Products. Information Relative to Prices, Profits and Competitive Conditions in the Tobacco Industry, Washington, D.C., 1922, 109pp. Also issued as 67th Congress, 2nd Session, Senate Doc. No. 121.

## TABLE OF CASES CITED

In the citation of Federal Trade Commission proceedings only the name of the respondent is given. In those instances in which no reference to the volumes of the Federal Trade Commission Decisions (cited F. T. C.) is yet available the complaint number is given together with the date of the order or dismissal where action has been taken.

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