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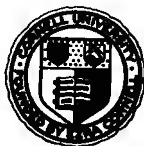

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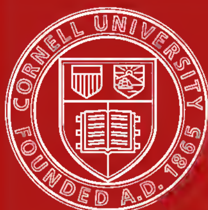

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EDITED BY

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TRUSTS, POOLS AND CORPORATIONS

EDITED WITH AN INTRODUCTION

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PREFACE

IN THE preface to the first edition of this collection of reprints in 1905 the distinction between its purpose and that of such predecessors as Dunbar's "Laws Relating to Currency, Finance and Banking" and Rand's "Economic History" was pointed out. This volume, according to its announcement, was intended for use especially as a textbook rather than for handy reference or as a collection of original documents. Similarly, it is hoped, this present enlarged edition is in no sense a rival, but rather complementary to such recent volumes as Stevens' "Industrial Combinations and Trusts" (1913) and Gerstenberg's "Materials of Corporation Finance" (1915). Each of these may greatly enrich instruction by affording a convenient store of well-chosen illustrative material. But this volume is intended to accomplish something more. It is a deliberate attempt to apply the case system, so successfully evolved in the Harvard Law School, to the study of economics. A systematic textbook, supplemented by lectures, is expected to provide the background so essential to a complete understanding of each selected case. But, this being done, most of these chapters purport to deal with a single, definite, typical phase of the general subject of industrial combination.

The primary motive is to further the interests of sound economic teaching, with especial reference to the study of concrete problems of great public and private interest. A difficulty in the substitution of present-day social and economic studies for the good old-fashioned, linguistic ones, or for the modern sciences, — a difficulty especially peculiar to descriptive economics as differentiated from economic theory, — has always been to secure data sufficiently concrete, definite and convenient to form a basis for analysis, discussion and criticism. The lecture system has its

advantages in stimulating interest and, it is to be hoped, arousing enthusiasm among students. But lectures alone entirely fail to do justice to the possibilities inherent in economic science for rigorously training the mind in habits of close and consecutive thought. The law has always enjoyed a peculiar and well-merited prominence among other studies for this reason.

The first requisite, therefore, for the successful conduct of economic instruction in the descriptive field is to provide raw material; which in discussion, supplementary to the general lectures, may be worked over in detail in the classroom. Such material, by reason of the great increase in economic periodical literature since 1890, is now rapidly augmenting. Yet with classes often aggregating in such economic courses from one to two hundred men, as at Harvard University, resort by each student to the files of such periodical literature is out of the question. Public documents are also impossible for reference reading with a class of considerable size. And finally, in my judgment, a generally neglected and amazingly rich find lies embedded in the mass of factual evidence accumulated in the course of legal proceedings in our courts. The mere decisions, as long currently used, are of course well known. But it is not the *legal* pronouncement in the case, infrequently interlarded with brief statements of fact, but the actual testimony adduced — "The Record" of evidence submitted — which has rarely been utilized. Such matter must be painstakingly uncovered, abridged, even digested, and made more conveniently accessible, to serve its due end for the teacher. To direct attention to this material by a few concrete illustrations from such sources, reprinted in this volume, is not an unimportant motive in its production.

A second incentive to the preparation of the original volume, ten years ago, was the hope that it might contribute to the crystallization of public opinion in favor of a fair policy of governmental control over monopolistic and corporate enterprises. This revised edition affords an opportunity to record the complete conviction of the people of the United States in favor of such a policy. The recent amendments of the Anti-Trust law in 1914

mark the formal entry of the Federal government upon a course of action imposing a grave responsibility upon its administrative agents. An understanding is needed, henceforth, not of the general principles of governmental control but rather of the application of that control to concrete instances of real or fancied abuse. The need of an annotated, *quasi*-official literature is insistent. By gathering together in convenient form this series of papers and documents it is confidently hoped that progress toward an understanding of one of our most troublesome public questions may be in some degree facilitated.

Both for the purpose of saving space and in order to avoid the appearance of discontinuity in the text, it has seemed best to eliminate many footnotes from the four hundred pages of new material added to this edition, as well as oftentimes to leave out all indication of solid omissions in the reading matter. The technical student under such circumstances is warned always to turn to the original article or document for detailed citations.

Acknowledgment is due to the editorial boards of the *Political Science Quarterly*, the *Economic Journal*, the *Yale Review* and the *Quarterly Journal of Economics*, and in even greater measure to the authors of the several papers herein reprinted, for permission to make use of their material in this enterprise. In every instance a most hearty acquiescence in the project has been expressed, for the which I cannot be too grateful. Without such assent the meagre original contributions of the editor would have made but a sorry show. To my former teacher at Columbia, President Goodnow of Johns Hopkins; to my former assistants at Harvard, Professors Tosdal and Dewing, and, with a peculiar sense of personal attachment, to my old friend Dr. Francis Walker, I wish especially to acknowledge indebtedness. This volume as it appears is largely the work of professional colleagues and friends. It is earnestly to be desired that the editor's endeavors may serve to direct attention anew to the value and interest of their contributions.

WILLIAM Z. RIPLEY

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INTRODUCTION

THE historical development of the so-called Trust Problem in the United States naturally falls into five more or less clearly defined periods. The revival of industry following the long depression of 1873–1879 began the modern development of large-scale production. Corporations embodying the principles of limited liability, delegated management and indirect ownership became increasingly prominent after 1880. The *first* period in our trust history may be said, therefore, to extend from about this time until 1887. It was characterized by a steady increase in the size and number of large-scale industrial units. Various pools and the Standard Oil Trust foreshadowed the future. The decade from 1887 to 1897 forms the *second* period. It was the time of the trust in the strict legal sense. Standard Oil Trust success since 1882 invited imitation in the two important industries of distilling and sugar refining. The progress of monopoly was such that an outbreak of state anti-trust laws from 1889 to 1893 indicated how fully public interest had turned from the regulation of railroads to that of industrial monopoly. It was assumed, in fact, that the railroad question had been in a large measure settled by the enactment of the Interstate Commerce Act in 1887. As instanced later in this brief review, the entire failure of the trust expedient, however, in furnishing a legal basis for monopoly led to various other devices, notably pooling. And the continuation of industrial depression, during the four years to 1897, rendered constructive development unlikely. The *third* period, from 1897 until the Northern Securities decision in the spring of 1904, was largely influenced by the phenomenal prosperity which began in the former year and culminated in 1902. The organization of combinations in various branches of iron and steel manufacture,

followed by the great outbreak of corporate promotion in 1899, led up to the formation of the U. S. Steel Corporation in 1901. This time it was the holding company, organizing under the laws of the charter-mongering states which seemed to offer a convenient substitute for the old and discredited form of trust.

The *fourth* period in the development of monopoly begins with 1902. It was characterized by sore trial and bitter experience, both economic and legal. Speculative scandals hereafter discussed; the panic and bankruptcies of 1903; the failure of bright promises of promoters; keen popular interest in railroad legislation and the tariff; each and all of them were accompanied by a growing demand for publicity. An outstanding event was the Supreme Court condemnation in 1904 of the device of the holding company in the Northern Securities case. In the same year the United States Bureau of Corporations was established and at once initiated an elaborate series of reports upon industrial combinations. Within two years after 1905 came, successively, the Hughes New York insurance investigation, the "Beef Trust," the Metropolitan Street Railway, the Harriman railroad and the Havemeyer sugar episodes. Suggestions of additional restrictive legislation came from the National Civic Federation, as well as from a number of Congressional committees. The tide of progressivism was evidently rising, manifested on all sides, concerning pure food, labor and transportation as well as industrial monopoly. The climax came in the vigorous application of the antitrust law by the Taft administration, which surpassed even the Roosevelt régime in its insistence upon strict compliance with the law as it then stood upon the statute books. The logical outcome of this mass of litigation was the great Standard Oil decision of 1911, which brought the fourth period in the development of the trust problem to a close. It unquestionably favored, if it did not actually necessitate, the legislation of 1914 with which the latest period in our chronicle is largely concerned. The full significance of that event will appear in due course.

During the generation which has now elapsed since industrial monopoly first took its rise in the United States, as it thus ap-

pears, a succession of distinct legal devices have been utilized as a basis for organization. In order of appearance these have been, the pool, the trust, the simple corporation, and the finance company or holding corporation.

The pool is probably the oldest, the most common and at the same time the most popular, mode of obviating the evils of competition. Industrial pools, in fact, appear at every stage of our economic growth since the Civil War. They are not even eliminated by gigantic mergers, so long as the latter fall short of complete monopoly. Thus even the most powerful present-day combinations, such as the United States Steel Corporation, have at times found it necessary to become parties to pooling arrangements with independent producers. The secrecy of these agreements, owing to a wholesome fear of the law, has rendered them apparently less widespread and effective than they perhaps were in fact. Such agreements may even be international in their scope, as shown by the allotment of the European export trade in steel rails in 1904 between the great German steel combination, known as the Stahlwerksverband,[1] and the English rolling mills. A seemingly undue amount of attention has been devoted to the subject of pools in this volume, because of their persistency and of the light which they throw upon the disadvantages of excessive competition.

A type of the earliest form of pool is afforded by the Michigan Salt Association, dating practically from 1868. As described hereinafter in detail,[2] this was an agreement for the purchase of the entire output of all the important producers in a certain field. Similar agreements were certainly operative in the decade 1880–1890, as in the manufacture and sale of cotton bagging, wherein was controlled perhaps two thirds of the output of the country. The most notable pools twenty years ago, however, arousing widespread attention, were in the distilling industry. In 1882 and even probably earlier, until the formation of the trust, a limitation of output and allotment of sales was cer-

[1] Described in Chapter XXIV, *infra*.

[2] Stevens, Industrial Combinations and Trusts, p. 1. ff., reproduces several such early agreements. The economic background is described in Ripley, Railway Problems (rev. ed.), p. 216 *et. seq.*

tainly relied upon to prevent undue competition.[1] The well-known pools in the cordage manufacture dating from 1860 are also cases in point. A far less defensible scheme from a moral point of view, revealing the possible evils inherent in pooling, is illustrated by the case of the Addyston Pipe Company. Our record of this combination[2] shows it to have consisted of an agreement among competing producers to fix a monopolistic price by means of fictitious bids, with a division of the field to insure complete local monopoly for each plant. More recently still, and developing a peculiar vigor since the failure of other attempts at monopolization, either by outright purchase or a holding company, were the pools in the iron and steel industry. These, as described in Chapter III, sought to promote stability of prices in a field peculiarly subject to violent industrial fluctuations. When reasonably and fairly administered, having due regard, that is to say, to the welfare of the consuming public, such agreements might well serve to steady prices; but when otherwise managed, rapaciously enhancing prices, such pools have miserably failed, with greater evils both to the public and their own membership than those whose prevention was sought. These pools are veritably protean in form, ranging from simple "business meetings with a social aspect" like the Gary dinners of 1897–1898 in the steel trade (p. 178), to the most elaborate arrangements like the Wire Nail Association of 1895–1896,[3] and the German Kartells, exemplified in this volume by the potash syndicate and the Stahlwerksverband.[4] These German pools, it will be observed, are all tolerated by the government under the law concerning monopolistic combinations.[5] The Prussian government actually participates as a syndicate member in the potash agreement. What a contrast in policy with that pursued by the United States!

A highly specialized form of monopolistic agreement known as the *patent pool* was apparently derived from the experience

[1] See pp. 22 *et. seq.*

[2] Pp. 78 and 533, *infra.*

[3] Chapter III, *infra.*

[4] Chapters XXIII and XXIV. The German coal Kartell is carefully analysed by Dr. Francis Walker in *Pubs. Amer. Economic Ass.*, 3d ser., vol. V., 1904.

[5] Chapter XX, *infra.*

of the wire nail combination, the details being worked out by the attorneys formerly in charge of that organization. Until it was brought to book finally in the bathtub proceedings, reprinted herein, the plan was extensively employed, with large profit to the managers. One office in New York alone managed something like fifty organizations of this type. The pool was at once rendered stable and enforceable by making use of the form, if not the substance, of patent privileges. Such patents as bore upon the process or commodity were first united in the hands of a single individual or corporation. All participants in business thereafter were controlled by means of licenses, under which royalties based upon sworn statements of production were turned in to a central treasury. Good behavior, — that is to say, the maintenance of prescribed prices and practices, — was enforced by deposits resembling in form the deferred rebate contracts of the British shipping rings. Thus under the bathtub agreement each licensee paid $125 monthly for the privilege of operating a furnace, on the understanding that $100 of this was to be paid back at the end of three months. This left, after the first four months, $300 continuously on deposit for the good behavior of each furnace regularly operated. Security aggregating almost $50,000 was in this manner given for a continuance of the established trade practices. The bathtub case, reprinted in Chapter XVIII, is chosen from among several because it affords the clearest exposition of the plan and also because its successful prosecution by the government brought a considerable series of pools of this type to an end. The entirely artificial nature of the plan is evident from the fact that the patent selected was not vital, but was utilized merely as a means to the end of effective restraint of trade. The abortive patent pool in the Portland cement business in 1911 affords another example in this regard similar to the bathtub case.

The common patent pool was so specious in character that it presented little difficulty to the economic analyst. But the case is quite different where widespread combination is based upon the ownership of patents which are really basic. For, as repeatedly held by the courts, a patent monopoly will be upheld only when it is essential and not when it serves merely as a

device to promote monopoly. Litigation over the use of the Selden patent in 1909–1911 by the Association of Automobile Manufacturers; in the United Shoe Machinery Co. prosecutions;[1] and particularly in the Eastman Kodak and Motion Picture companies decisions of 1915,[2] respectively, afforded opportunity to test the fine distinction between the rights of patentees in inventions and the interest of the public in the perpetuation of a fair and open field for trade. The marked dissimilarity in circumstances between these various cases indicates the need of clearer definition of the conflicting rights of individuals and of the people at large. Patent rights should not be used as a shield to nullify the Sherman Act; and yet, as held in the shoe machinery case, it may be no offense to aggregate patents to such a point that practical monopoly results. Until the Supreme Court shall pronounce finally upon these matters the cases selected in Chapter XVIII appear best to embody the state of judicial opinion.

Obvious as are the advantages of successful pooling contracts to producers, they suffer from two inherent defects. The first of these is that they are at variance with the underlying principles both of common and statute law, and hence are not enforceable in the courts. No effective guarantee for good faith is afforded other than by the mechanism of deposits, the imposition of fines and other more or less clumsy devices. And a second objection lies in the fact that pools are necessarily but temporary expedients after all, affording no certainty for stability of price or of industrial policy over any extended period. It was undoubtedly conviction upon these points which led to the attempts in the late '80's to remodel industrial combinations on the pattern of the Standard Oil Trust of 1882. On the other hand it may perhaps be affirmed rightly that the very indefiniteness and elasticity of these pooling agreements has often rendered them successful when more rigid devices would have proved somewhat ineffective for the control of prices in the face of a rising tide of independent production.

An express *trust* may be defined as an organization managed

[1] 222 Fed. Rep. 349.

[2] 226 Fed. Rep. 62, and 225 Fed. Rep. 800.

by a board of trustees to which all the capital stock of the constituent companies is irrevocably assigned; in other words, the original shareholders accept the trustees' certificates in lieu of former evidences of ownership. The outline of a typical trust hereinafter printed will serve as an illustration.[1] As a legal expedient for obviating competition, such a trust is usually discussed as if it were now obsolete, possessing historic interest alone. This is only in part true. As an improvement upon the pool, both as regards stability and effectiveness, certainly it merits the importance ascribed to it during the decade following 1887. The first appearance of this legal expedient dates, of course, from the formation of the Standard Oil Trust in 1882.[2] It derived added prominence through the formation of the Distillers and Cattle Feeders' Trust (whisky) and the Sugar Trust, both in 1887. It disappeared with the final judicial condemnation under adverse state and Federal legislation in the years 1891–1892. The decision in the case of the North River Sugar Refining Co. and the Standard Oil Co. in Ohio, finally proved the impossibility of this legal basis for effecting combinations.[3] Recourse was necessarily had, therefore, to novel expedients, such as corporate organization under the newly revised laws of New Jersey and other charter-bartering states.

It is an odd coincidence, that organization under a board of trustees issuing certificates representative of ownership of property, although condemned by the courts and obsolete as a resource for the great industrial combinations of the country at large, should still flourish under the laws of Massachusetts. This commonwealth has, in the main, steadfastly resisted pressure for a loose, or even for a very liberal policy in corporate legislation; yet it is conspicuous among the other states to-day as permitting the trust form of organization to flourish. This is perhaps indirectly an outcome of the traditional policy of the state not to permit the holding of real estate for investment by

[1] Consult Chapter II, pp. 22 *et seq.*

[2] Pp. 554, *infra.* Miss Ida M. Tarbell's study of the Standard Oil Co. gives full details concerning both the form and dissolution of this trusteeship.

[3] *Vide* p. 465, *infra.* Both decisions are reprinted in Stevens, *op. cit.*, chapter IV.

corporations organized under its general laws. Moreover, this latter practice would be difficult under the common law rule against perpetuities. For more than half a century, therefore, real estate in Boston, if held for permanent investment by a number of people jointly, was compelled to vest its title in voluntary associations, managed by trustees. An important ruling of the Massachusetts supreme court in 1899, upholding the validity of such associations, greatly enhanced their prestige. At one time there were no fewer than sixty real estate trusts in the city of Boston alone, holding upwards of $60,000,000 of property.

The immunity from governmental supervision of voluntary associations under trusteeship, especially as regards the issue of capital stock, under the strict Massachusetts anti-stock-watering laws applicable to corporations, has latterly invited an extension of the principle of voluntary association into the fields both of transportation and industry. Thus the Massachusetts Electric Companies, controlling the stock of several hundred miles of street railways throughout the eastern part of the state, is managed through a board of trustees.[1] The board issues certificates representing the equitable interest of the original stockholders of the constituent companies comprehended within the enterprise. This, it will be observed, is quite analogous to the device originally adopted by the original sugar and Standard Oil combinations. The Massachusetts Gas Companies in the industrial field have likewise, as the virtual successors of the New England Gas & Coke Co., acquired control of the illuminating plants in and about Boston. In the field of private enterprise, there was a reorganization in 1911 of the Amoskeag Manufacturing Company, owning the great cotton mills at Manchester, N. H., as a voluntary association under the laws of that state. Its former capital stock of $6,000,000 is now represented by participating certificates having no par value, exchanged at the rate of two for each old preferred share and three for each common share.[2]

[1] Gerstenberg, Materials of Corporation Finance, pp. 10 ff., reproduces its declaration of trust in full.

[2] The prevalence of these voluntary associations brought about a special investigation by the Tax Commissioner of Massachusetts in 1912–1913: Mass. House doc. No.

The Ludlow Associates similarly operate very large textile plants in Massachusetts as a voluntary association. It thus appears that the legal principle of trusteeship is by no means obsolete; although the device has in no guise been revived for the purpose of consolidation in any great staple interstate industry.

The *holding corporation* came into vogue in the late '90's as the legitimate successor of the discredited trust; but the languishing condition of American industry for several years following the panic of 1893–1894 retarded whatever further tendency toward consolidation might then have occurred. The resumption of trade activity in 1897 once more revived the forces making for combination. At the same time the renewal of confidence among investors, following the protracted period of speculative dullness, created novel and unforeseen opportunities for industrial promotion.[1] The phenomenal outburst of combination which took place during the two years following 1899 was largely based upon the use of this new legal expedient, the holding company. Until about 1870 in England, and twenty years later in our own country, the weight of legal authority had been adverse to the holding of the stock of one corporation by another. Railroads for a generation had, by special provision of law, controlled subsidiary companies in this way.[2] But the passage of a new corporation act by New Jersey in 1889 first legalized the practice under general statutes. Vast possibilities were involved in this fundamental change in American corporation law. Companies could hereafter be organized as well to serve the ends of bankers and promoters as those of industrial efficiency. The New Jersey type of corporation need have no operating duties whatsoever, other than to hold the shares of other concerns, elect officers, receive dividends from constituent companies and turn them over to their own stock or bond holders. It was necessary merely to maintain a nominal con-

1646, 1912, and No. 1788, 1913. The Secretary of State now publishes annually as a state document, the text of all such voluntary agreements. A. D. Chandler, Express Trusts under the Common Law, 1912, is worth consulting.

[1] The extraordinary combination of influences at work in this period are best described in the *Quarterly Journal of Economics* for February 1905.

[2] Ripley, Railroads: Finance and Organization, pp. 433 ff., gives details.

nection with the chartering state by renting desk room, displaying a sign, going through the form of an annual meeting and rendering meager annual reports.[1] Many American commonwealths, notably Delaware, Maine, West Virginia and North Dakota, promptly followed the example of New Jersey, profiting greatly thereby from the resultant fees. Only two states seem to have wholly resisted the temptation to authorize the holding company by the amendment of their industrial codes.

The advantages, financial and operating, of the holding company were apparent from the start. It facilitated the promoter's task; inasmuch as only a small proportion of stock in each constituent corporation need be purchased in the open market in order to give control. Formerly the acquisition of the last few outstanding shares of a company at private sale was a stumbling block in the way of combination. Territorial and operating division of the business was much easier, where the various parts might each be assigned to a separate corporation. The individuality of constituent concerns, trade-marks, good will, and the like, might be perpetuated, along with the stimulation of personal interest and zeal, by leaving a considerable fraction of the stock ownership in subsidiary companies in the hands of the original owners. Even the difficult task of apportioning the business among a number of rivals might be accomplished by having all competitors represented as shareholders in a central organization. Thus did the National Packing Co., the National Electric Lamp Co., and the Temple Iron Co. promote industrial peace and good will under virtual monopoly in the beef, the electrical manufacturing, and the anthracite coal businesses, respectively. Yet relatively few concerns seem to have taken advantage at once of the means made ready to hand by the New Jersey legislature. The American Cotton Oil Co. in 1889 and the United States Rubber Co. four years later, were pioneers. The time was propitious in many ways, except for the prevalent industrial dullness. The prospect was rendered inviting legally, by the attitude manifested toward combination by the United

[1] The use of a Maine holding company in the affairs of the thousands of miles of railroad system in Brazil is an extreme example of such practice. Lowenfeld criticizes it in *Finance-Univers*, Vol. IV, June 15, 1915, p 1.

States Supreme Court in 1894 in the Knight case. But the heyday of the holding company did not dawn until the outburst of industrial promotion in 1898, to which reference has already been made. The success of the first combination in the iron and steel business, the Federal Steel Co., pointed the way. Further impetus was given by the demonstration that if the terms of exchange for capital stock could be so arranged that the new shares had an apparent money value greater than that of the old certificates, the owners might be depended upon to "act naturally like a flock of sheep."[1]

For a brief period, owing to the advantages above mentioned, the holding company device assumed peculiar prominence in almost every branch of American business life. In mining, the Amalgamated Copper Co.; in merchandising, the Associated Merchants Co., with a made-over charter from Connecticut of the Columbian Construction Co., empowering it "to conduct any lawful business"; in transportation, the Northern Securities and the Rock Island companies for interstate business and a host of other combinations in the public utilities field within the separate states, — were all built upon the principle of a parent corporation which controlled its subsidiaries by means of stock holdings. Without this device the United Steel Corporation, — the climax of the whole movement, — with its aggregate capitalization of $1,400,000,000 would have been impossible, to say nothing of the great tobacco combination constructed upon the same model. A minor outbreak of promotion occurred in 1908–1909 which brought into being a new crop of merchandising combinations and of such manufacturing concerns as the General Motors Co. Here again the holding corporation served to bind the various parties together.

By this time experience had demonstrated a large number of disadvantages inherent in the departure from the established legal practice that one corporation should not be permitted to hold stock in another. Investors refused longer to act like a flock of sheep, and began to discriminate between immediate and remote ownership of tangible property. The new practice was

[1] Pamphlet, Holding Companies, by Robert F. Herrick, Esq., Boston, Jan. 20, 1909. Cf. p. 277, *infra*, on the Consolidated Tobacco Co. experience of 1901.

too apt to invite what Dewing characterizes as an "almost hopeless tangle of direct, indirect and contingent liabilities." This occurred in such unfortunate enterprises as the New England Cotton Duck, the United States Realty and Construction and the American Malting companies. The invitation to the manipulation of accounts and to secret profits for insiders is exemplified in our reprints dealing with the affairs of the ship-building combination.[1] "The division of individual responsibility," as Dewing puts it, the divorce of control and responsibility from real ownership, the evil of padded accounts and particularly of the consolidated balance sheet, the conversion of contingent stock liability for dividends into fixed charges upon bonds, all demonstrated anew the danger to investors lurking in this radical departure from precedent. Furthermore the people at large were now taking a hand. The Northern Securities decision frowned upon the device in railroading. Legislative proposals, even to the extent of absolute prohibition of the practice, threatening to render the holding company vulnerable in the courts, finally resulted in the prohibition of the practice of intercorporate stock holding altogether by New Jersey, the pioneer, in 1913. Is this the beginning of the end or not?

One of the gravest financial objections to intercorporate stock holding is the ease with which a minority of stock ownership may perpetuate itself in control by means of a series of holding companies one upon another. Where the holding company owns practically all of the stock of the constituent corporations this evil is absent. In the Steel Corporation, the Agricultural Chemical Co., or the General Motors Co., there are practically no minority stockholders whose rights may be jeopardized. But the principle once admitted, there is no limit to the amount of involution; nor is there any safeguard against downright oppression of a large majority of shareholders by the few. Thus the United States Dry Goods Companies under the laws of Delaware controls the Associated Merchants Co., with a Connecticut charter empowering it to conduct any lawful business; while it in turn dominates the H. B. Claflin Co. of New Jersey through the ownership of 45,001 out of 90,000

[1] Chapter XII.

shares of stock. Under such circumstances what becomes of the essential obligations of managers to investors, to say nothing of the relationship of so devious a concern to the authorities of the different states?[1] Fortunately the trend at the present time is distinctly away from both the holding company and the practice of incorporation in the charter-mongering states. Many concerns are simplifying their corporate structure. The Amalgamated Copper Co. in 1915 resolved itself into its constituent parts. The American Malting Co. is about to abandon its holding corporation. The American Woolen Co. has just deserted New Jersey and returned to Massachusetts, corporatively, where it belonged. And a number of other concerns now manifest a disposition to follow suit. The pure finance corporation may in time, as it deserves, come to be a specimen for preservation in economic museums.

The trust movement has brought to light a number of evils in corporate finance, or rather it has magnified preëxisting tendencies which had been apparent only on a small scale. The principal ones in our experience are imprudent or fraudulent promotion and subsequent speculative management. It is difficult at all times to draw the line clearly between recklessness, inefficiency and dishonesty. But a vast increase in irresponsibility of corporate management has certainly paved the way to financial practices which are highly objectionable, if not criminal. The examination of such matters forms part of any comprehensive treatment of the corporation problem.

The *promotion* of an industrial enterprise is a chancy operation at best. Where it is undertaken on behalf of others, that is to say, involving the use of their funds rather than the employment of the promoter's own capital, an added premium is set upon imprudence. Certainly many of the promotions of the period 1900–1901 impress the onlooker as unwise in the extreme. On the other hand, there is of course a substantial economic defense for the payment of large returns to those who incur the risks of novel enterprises. But even with full allowance

[1] Cf. Dewing's diagram of the organization of the glucose combination. *Op. cit.*, p. 111.

therefor, the returns of both organizers and banking syndicates during this period seem to be excessive. Where promotion occurred from within as in the harvester organization,[1] no ground for criticism is afforded. More debatable is the warrant for the large returns which accrued to underwriters in the promotion of the U. S. Steel Corporation.[2] In a different group belong the reprehensible practices in promotion, which merit the name of downright theft. Two notable instances are described in this volume by the official reports of receivers for the asphalt and shipbuilding combinations, respectively.[3] The veil of secrecy thrown about the promotion of the Amalgamated Copper Co.[3] has been sufficiently lifted at times to warrant the belief that exorbitant profits were made in this instance. Nefarious practices of this sort have already been condemned by the courts in several notable instances of late.[4] But the removal of the incentive to reckless promotion through stringent regulation of the conditions of flotation, as is done in the excellent German law described herein,[5] would seem to afford complete protection.

The *payment of unearned dividends* is another evil which in the past has not been curbed by a series of decisions in our American courts attempting to distinguish clearly between capital and income accounts. Nice questions of policy are involved in the determination of net profits. An unwise practice of many industrial combinations in failing to provide sufficient reserves before beginning the payment of dividends has frequently precipitated bankruptcy. Most unfortunately, downright deception often merging into fraud has at times been adduced in evidence. The asphalt companies clearly exemplify the lack of a conservative policy in accounting; as when, for instance, the Audit Co. of New York changed an apparent surplus of $758,000 to a deficit of $541,000. The United States Realty

[1] Pp. 324 and 634.

[2] Pp. 169 and 203.

[3] Pp. 203 and 439. Dewing, *op. cit.*, is the standard authority on matters of this character.

[4] On the liability of promoters for unrevealed profits, consult the review of cases by the editor in the *Journal of Political Economy*, Vol. VIII, 1900, pp. 535 *et seq.*

[5] Chapter XXII, p. 774.

Co. is another case in point. Dividends were here paid on the basis of profits on uncompleted contracts, recalling the similar policy in the case of the U. S. Shipbuilding Co.[1] Numerous other concerns have since been known to have followed the same practice, notably the New England Cotton Yarn and the Virginia-Carolina Chemical Co. Perhaps the worst offender was the American Malting Co., in a case so extreme and so clearly fraudulent that the courts in 1905 held the directors liable both to creditors and stockholders to the full amount of the unearned dividends declared.[2] It is earnestly to be hoped that a few more judgments of this kind will serve to restrain the directorates of other great corporations.

The evil of *speculative management* falls into several distinct parts. The earliest form which it took was the buying and selling by its own officers of the securities of a corporation for speculative purposes. Of this sort are the events in the history of the Whiskey Trust, and a few scattered instances such as the manipulation of Diamond Match funds in 1896. American corporations, unlike those of England and Germany, fail in too many instances to prohibit dealings in the securities of a company by its own officers. The best of them certainly do so, and the scandals of a decade ago probably emphasized the desirability of preventing this evil. An unlimited power to contract loans without the approval of the directors or stockholders, as in the case of the American Ice Co., is also a constant menace to conservative management. Another phase of this matter concerns the temptation to industrial management with a view to its effect upon the stock market rather than upon the permanent welfare of the company. A classic example is afforded by the episode of the American Steel & Wire Co. in 1900. Secrecy is a constant invitation to the insider to take advantage of forthcoming events at the expense of the stockholders. It is undeniable also that such speculative management greatly encourages speculative ownership on the part of stockholders. The old-fashioned investor, secure in his belief in the stability of his company, is replaced by a body of temporary holders

[1] Pp. 403 *et seq.*

[2] Dewing, *op. cit.*, ably reviews this experience.

who look for the returns upon their investment more in the chances of buying and selling and manipulation, than from permanent and regular dividends. That this kind of ownership is greatly encouraged by the very low quotations of the stocks of overcapitalized companies cannot be doubted.

The spread of the practice of indirect ownership through the mediation of holding or finance companies has also produced a peculiar set of abuses. These are all dependent in the main upon the preservation of secrecy as to the exact status of the operating concern. Dividends or deficits may be shifted at the will of the directors from one to another company of the hierarchy. Only when disclosure is forced by financial stress or judicial proceedings is the real state of affairs revealed. Our reprint of the Receiver's report of the United States Shipbuilding Co. serves to illustrate this evil.[1] Other instances of the creation of large floating debts by constituent companies, which debts are not apparent in the reports of the parent concern, are familiar in the case of the United States Rubber Co. and the New England Cotton Yarn Co.[2] The failure to disclose may, however, at times operate in the other direction. Stock-holders are induced to sell because of failure on the part of the management to make clear the accumulated profits of constituent companies. This would seem to be exemplified in the recent history of the companies which constituted the so-called Tobacco Trust. On the formation of the Consolidated Company in 1901,[3] the majority of the common stocks of the American and Continental Tobacco companies were taken over in exchange for four per cent collateral bonds. The holders of the non-dividend Continental stock parted with their property without any knowledge whatever of the profits which it had been earning. Only after they had been given in exchange a security with a fixed return, did it appear that very large profits had accrued. In

[1] Pp. 403 *et seq.* Cf. also the unhappy experience of investors in the National Lead Co. in July, 1910 and in the U. S. Finishing Co. in 1913. In the latter case, there was speculation by subsidiary companies both in merchandise and in its own securities, resulting in losses which aggregated $1,250,000.

[2] *Cf.* the *N. Y. Times Annalist*, July 5 and 19, 1915, on the abominable rubber stock operations, and the views prevalent among directors of other concerns.

[3] Pp. 277 *et seq.*

fact, the dividends of the Continental Co. were soon increased to ten and afterward to sixteen per cent. The profits to those who had assumed control of the Consolidated Company were correspondingly great; inasmuch as they received all the surplus income over the fixed returns given in exchange for the old securities. It is the possibility of such shuffling as this which rendered the bonds of the Consolidated Company so unpopular that the entire plan had to be revised.

Excessive capitalization in proportion to tangible assets and earning power, according to public opinion, is one of the most common and persistent defects in American corporate organization, especially among industrial combinations. Consumers allege that while there is no directly traceable relation between capitalization and prices, an excess of securities craving dividends is in itself an indirect incentive to unreasonable charges. However true this may be of public service or other natural monopolies, so many factors not financial enter into the determination of the market prices of most commodities as largely to invalidate this contention. Was not the Standard Oil Co. until very lately one of the most modestly capitalized "trusts" without any evidence of an effect upon its price policy toward consumers? Yet it is probably true, nevertheless, that the absence of definite correlation between assets and capital liabilities is a source of confusion to all parties concerned. It may conceal unearned profits of promoters or subsequent mismanagement by directors. It is an invitation to speculation both within and without. It is the negation of fair and reasonable publicity. Overcapitalization is, to be sure, more often merely a symptom of disorder than a disease in itself. And it is certainly the nature of the securities outstanding rather than their aggregate amount which is provocative of trouble. Dividend obligations contingent upon earnings do not precipitate trouble as do heavy burdens of fixed charges upon bonds or notes. Yet the constant association of an excessive issue of securities with financial distress renders a conservative policy in this regard almost an index of financial stability.

Most of the industrial promotions of 1899–1901 were seriously open to the criticism of overcapitalization. The belated experiment of the International Mercantile Marine Co., included in

these reprints, was the climax of reckless financiering in this regard.[1] It is reported that reorganization, now pending under receivership, is to cut the outstanding body of securities in halves. An equally drastic pruning of the capitalization of the American Malting Co., the source of whose troubles was imprudent finance, has just been announced. Quite a number of large companies have voluntarily, or in the process of reorganization, reduced the volume of their outstanding securities. The National Lead Co. in 1891 reduced its capitalization from ninety to thirty million dollars. The Distillers' Securities Corporation now has less than half the amount outstanding against its predecessors. The New England Cotton Yarn Co. by one stroke eliminated the good will item from its accounts, thereby reducing the totals on its balance sheet by about five million dollars. The American Ice Co. represents its condition in the following words of its own president: "It is clear that the capitalization is excessive; that the common stock represents no earning capacity even under normal business conditions." Other recklessly promoted companies now find themselves similarly placed.[2] It is clear that the danger of overcapitalization is being impressed upon all parties concerned. Experience has proved indubitably that in the long run the conservatively capitalized companies can far better command bankers' credit, weather periods of financial strain and hold the allegiance of investors. Little more than publicity and standardization of accounts would seem to be essential to safeguard whatever interest the public may have in the larger industrial enterprises of this sort.

The prime interest of the general public in the maintenance of *reasonable prices* is comprehended in these reprints by a number of separate discussions. Originally and for many years it was believed that an extortionate price policy was the invariable accompaniment of combination. This resulted in all probability from the success with which the petroleum, beef and sugar

[1] Experience to 1915 is described in *Journal of Political Economy*, XXIII, pp. 910–926.

[2] *Cf.* the checkered career of the New England cotton duck combination; Dewing, *op. cit.*, chapters XIII and XIV.

"trusts" augmented prices to consumers while coincidentally, as it appeared, depressing prices to the producers of raw material. There is little doubt that complete control of the market usually leads to such conclusions. Experience with the wire-nail pool of 1895, the bathtub, watch case and other concerns[1] confirms this opinion. But, on the other hand, some of the strongest combinations seem to have abstained from pursuing an extortionate price policy at all. The Steel Corporation has an enviable record in this regard, as described in our reprint of the Federal decision in Chapter V. The avoidance of an undue depression of prices as well as of an excessive increase seems to have been the end in view. The International Harvester Co., also, as represented in these reprints, is not open to the charge of unduly enhancing the prices of its products. As for the tobacco combination, while prices seem not to have been affected appreciably either before or after dissolution, it is clear that any reduction following the removal of internal revenue taxes was prevented.[2] Another question respecting prices concerns the welfare of competitors. It is unquestionable that arbitrary manipulation of the market both as between persons and places has greatly contributed at times to drive out wholesome rivalry in trade. And the specific prohibition of local price discrimination in the Clayton Act of 1914[3] is intended to safeguard the public interests in this respect. The latest decisions of the Federal courts interpreting the Sherman Act have at all events concluded that a "free and untrammeled traffic of the marketplace," regardless of the particular course of prices, must be perpetuated at all hazards.

Unfair competition is a term descriptive of practices which have been disclosed in connection with a number of prosecutions of monopolies in recent years. The leading authority upon the subject[4] enumerates eleven different forms, among which are the operation of bogus "independent" concerns; the mainte-

[1] Pp. 46, 606 and 655.

[2] Pp. 313 ff.

[3] P. 715.

[4] W. S. Stevens, *Political Science Quarterly*, XXIV, 1914, pp. 282–306 and 460–490. These are enumerated also in the La Follette bills, reprinted by Stevens, *op. cit.*, p. 530.

nance of "fighting brands," cheaply contrived in order to put competitors out of business; blacklists and boycotts; espionage and the employment of detectives; manipulation of the market; rebates; preferential contracts and the like. The cases reprinted herein illustrate but a part of these; although so far as they go they clearly betray the jealous regard by the state for the rights of weaker competitors in trade. Noteworthy among our chosen illustrations of unfair practice, are the following: the bathtub and Keystone Watch cases, with intimidation and espionage; the International Harvester Co., with the employment of bogus or secret independent concerns in the early days; and most predatory of all, the National Cash Register Co., with its use of coercion in the most flagrant forms. Not all these unfair practices are specifically defined in the amendments to the Sherman Act, of 1914, soon to be discussed; but a clear appreciation of their tangibility and occasional enormity is essential to an understanding of the pressing need for prohibitive legislation of some sort. The courts, interpreting the Anti-Trust law, had so variously and conflictingly defined the rights of competitors, that the business man was left in doubt as to what tactics he was lawfully entitled to adopt in trade; while the public on its side was offended at the likelihood that force might entirely supplant ability and efficiency as a means to commercial success.

The existing *legislation* by the United States for the regulation of monopoly is reproduced in this volume in the text of the original Sherman Anti-Trust Act, and of the enactments of 1914 known as the Trade Commission Law and the Clayton Act.[1] Their history is epitomized in each case by means of the appended editorial notes. So much of the meaning of this legislation, owing to its original brevity, has arisen from subsequent interpretation in the Federal courts that it has seemed best to devote a considerable space to that subject. In Chapter XV the history of the original legislation and its application to common carriers is traced; while the remaining decisions prior to 1901 are given in Chapter XVI.[2] The editor's notes

[1] Pp. 485, 704 and 715.
[2] P. 550.

summarize the development preceding the Standard Oil decision in 1911, primarily in order to show how very widespread the application of the law came to be. Few branches of trade in the United States were wholly immune from prosecution. Yet while the law was being so actively enforced, no affirmative construction of the statute by judicial proceedings ensued. A hit-or-miss policy was pursued by the Department of Justice. But at last, as set forth in the introduction to Chapter XVIII, the necessity of squarely facing the great issues involved was presented by the Standard Oil case. Was the statute to be interpreted as utterly prohibiting combination in any form; or was a meaning to be read into it which should permit somewhat of the liberty which the laws of continental countries allow? The background for an understanding of this decision is constituted by our reprints dealing with the English common law concerning monopoly and the restraint of trade.[1] The established policy toward combination adopted in the continental countries of Europe is outlined in Chapter XX. According to French law, as it appears, only such combinations as conspire to advance prices above a competitive level are prohibited. In Austria there is no criminal penalty against combination; but, as by the English common law concerning restraint of trade, the protection of the courts is withdrawn from such agreements, thereby rendering them null and void. The German practice, by way of contrast, accords complete validity at civil law to combination in lieu of prohibition. This validation of pooling and other devices it seemed best to describe fully in the two concluding chapters. The German potash and steel syndicates embody practically all of the essential details of organizations of this sort. One of the first tasks set for itself by the new Federal Trade Commission being to organize the American export trade, the domestic policy of these foreign countries becomes to the United States a matter of international concern.

[1] Pages 453, 475 and 561. Cf. also *Harvard Law Review*, Vol. XVII, pp. 156 and 217. The English decisions and also the text of the British Companies Act is reprinted in convenient form by our House Committee on Judiciary as "Laws on Trusts and Monopolies, Domestic and Foreign," January 10, 1914.

Many other plans for dealing with the problems of monopoly and large-scale business, other than the one finally embodied in the statutes of 1914 here reprinted, were brought forward during the decade of active discussion of the subject. Federal incorporation was formerly advocated in high quarters;[1] and federal license on condition of good behavior was also warmly espoused.[2] In view of the decisive step taken by Congress one need not inquire whether these plans were adequate or impracticable; nor whether judicial control alone in place of continuous administrative supervision might have supplied such regulation as the abuses of the time seemed to require.[3] The Supreme Court of the United States has declared that the anti-trust law of 1890, "embraced every conceivable act which could possibly come within the spirit or purpose of prohibitions of the law, without regard to the garb in which such acts were clothed. . . . There was no possibility of frustrating that policy by resorting to any disguise or subterfuge of form, since resort to reason rendered it impossible to escape by any indirection the prohibition of the statute."[4] Uncertainty still prevails only as regards "all those normal and usual contracts essential to individual freedom, and the right to make which was necessary in order that the course of trade might be free." The extent of this exception, inserted, if you please, in the act by judicial construction merely, in accordance with the rule of reason remains yet to be defined. But on the whole it would seem to give scope to such activities in business as are fair and reasonable even though they may incidentally diminish competition to some degree. The rigid strait-jacket in which American trade and manufacture found itself before the Standard Oil decision of 1911 and the amendments of the Sherman Act in 1914 has been loosed, in order to permit of such growth and freedom of action as are compatible with the best interests of the community at large. The mandate

[1] President Taft's message of 1911; Report of Commissioner of Corporations, 1904; *Harvard Law Review*, Vol. XXVI, pp. 667–683, and *Michigan Law Review*, Vol. II, pp. 358 and 506.

[2] U. S. Commissioner of Corporations, 1904, 1906 and 1909; National Civic Federation, 1908, 1913.

[3] *Harvard Law Review*, Vol. XVII, 1904, pp. 156–247.

[4] P. 595 *infra*.

given to the newly created Trade Commission to prescribe the precise degree of this relaxation of restraint is a most general and sweeping one, — not less so than the order to the Interstate Commerce Commission to prevent all "unreasonable" rates and practices. How fully this body will respond to the summons, and actually contribute to the standardization of business practice in the United States upon a higher plane both of ethics and of efficiency, time alone will reveal.

WILLIAM Z. RIPLEY

TRUSTS, POOLS AND CORPORATIONS

I

THE MICHIGAN SALT ASSOCIATION[1]

WITHIN the last half century, the amazing comparative growth of capital as a factor in production; the combinations of workingmen arising from their forced association in manufacture according to modern methods, and the ensuing discontent — or rather, the frequent and increasingly emphatic expression of discontent — with their lot on the part of the workingmen, as combination has increased their sense of strength; the combinations of capitalists and the startling revelations of power afforded by such organizations as the Standard Oil Company and the coal syndicates of Pennsylvania, — all these things have lent to the study of combinations among either capitalists or workingmen, or of coöperative unions of the two, an especial interest. More frequently the subject has been studied with reference to workingmen, the advantages and disadvantages to them; but it seems no less desirable, from the standpoint of the economist at least, that combinations among capitalists, either for purposes of protection against unreasonable demands of workingmen or for their own interests as producers, should be studied; and that the investigation should cover the influence of such combinations on the consumers as well as upon the capitalists themselves.

The story of the Standard Oil Company has been told more than once, in words eloquent with the conviction of the danger threatening our government and civilization from the growth of such corporations. The consumers of anthracite coal throughout the United States during the past two years, have needed

[1] From the *Political Science Quarterly*, Vol. III, 1888, pp. 78–98. For additional references, see footnote on p. 21 *infra*.

no publicist to tell them that some powerful influence has been brought to bear upon the price of this product. Although far less in power than either of the combinations mentioned, the Michigan Salt Association, from the extent of its influence over the price of an article of food so common and so necessary as salt, as well as from the magnitude of its operations and its great and apparently increasing power, seems to be a fit subject for a study of this kind. The extent of the influence of the association may be noted, when we consider that Michigan produces more than 40 per cent of all the salt manufactured in the United States, and that, of the Michigan product, not far from 95 per cent will be sold by the association during the coming year. In short, speaking generally, the price of the salt consumed in all the Northern states west of Pennsylvania and New York, until we approach those bordering on the Pacific ocean, is the price set by the managers of this association. It is the purpose of this article to give a short sketch of the history of this combination of manufacturers, with that of others which preceded it; to describe its plan of organization and its work, and to estimate the influence which it has exerted and that which it can exert on the price of salt.

The early settlers of Michigan had learned from the Indians of the existence of many salt "licks," or springs, in different parts of the state, and it was thought even by them that there was an opportunity for the growth of a great industry in its manufacture. In 1838 Dr. Houghton, the state geologist, called the attention of the legislature to these facts, and suggested that an appropriation be made for the sinking of test wells. The time was propitious for such a request. The newly adopted constitution had declared: "Internal improvements shall be encouraged by the government of this state;" and the governor had been authorized by the ambitious first legislature to borrow on the credit of the state the sum of $5,000,000, to constitute an internal improvement fund.[1] From this fund $3000 were at once appropriated; the next year $15,000 more, and small sums in succeeding years. While salt was found, the wells were not sunk deep enough to yield brine in paying quantities.

[1] Cooley, Michigan, ch. xiv. [American Commonwealth Series.]

In 1859, an act was passed exempting from taxation all property used in the manufacture of salt and offering a bounty of ten cents per bushel on all salt made in the state. A corporation, the Saginaw Salt Manufacturing Company, was formed the same year in East Saginaw to put down a well and engage in the manufacture of salt. So little was known, even by the board of directors and officers of the company, regarding the character of the work, that it was necessary for a committee to visit the Onondaga salt works to learn what buildings, machinery, and tools were necessary for boring the well. But by February 7, 1860, the directors felt warranted in making a report to stockholders, declaring the work a success. In March the well was completed; another one was immediately put down; and manufacture began in July. The works were thrown open for inspection July 4. In this first year, 1860, about 4000 barrels of salt were manufactured.[1]

As soon as it became known that brine of paying quality and quantity was to be found in the valley, capital was rapidly invested. In 1862, 243,000 barrels were made, and in six years there were engaged in the manufacture of salt in the Saginaw valley, sixty-six different companies with an investment of nearly $2,000,000.

TABLE I

ANNUAL SALT PRODUCT OF MICHIGAN, 1860–1886

YEAR	BARRELS	YEAR	BARRELS
1860	4,000	1874	1,028,979
1861	125,000	1875	1,081,865
1862	243,000	1876	1,462,729
1863	466,356	1877	1,960,997
1864	529,073	1878	1,855,884
1865	477,200	1879	2,058,040
1866	407,077	1880	2,676,588
1867	474,721	1881	2,750,299
1868	555,690	1882	3,037,317
1869	560,818	1883	2,894,672
1870	621,350	1884	3,161,806
1871	728,175	1885	3,297,403
1872	724,481	1886	3,677,257
1873	823,346		

[1] Statistics relating to the Saline Interests of Michigan, by S. S. Garrigues, Ph.D., State Salt Inspector; Lansing, 1881.

This table shows, in the falling off of the yearly product, 1865–1867, the result of the rapid and in many instances ill-advised investment of capital. Under the conditions obtaining at the time, unrestricted competition soon drove the weaker companies to the wall. In those days, the extent of the salt-producing territory and the methods of manufacture were less well known, and the business was much more of a natural monopoly than now. Under these circumstances, the solution of the difficulty was evident: combination was indicated and combination soon appeared. In a statistical summary of the leading products of the Saginaw valley, published by *The Saginaw Daily Enterprise* in 1867, we read: "This interest [salt] is somewhat under a cloud at present through the evil influence of speculation and inconsiderate management." Then, farther down the page come, as one might expect, the words: "At least two-thirds of those [blocks] now running turn in their production to the Saginaw Salt Company." Thus, as early as 1866, six years only after the industry was started, we find that many of the manufacturers were uniting their interests so far as the sale of the product was concerned.

Soon, from individual agreements the leading firms came to something more stable and far-reaching in its influence. On the 16th of April, 1868, the articles of association of the Saginaw and Bay Salt Company were adopted. The first year of its existence, this association handled four-fifths of all the salt shipped from the Saginaw valley. Its benefits to the manufacturers, as well as to the consumers, — so far, at least, as the quality of salt is concerned, — were at once recognized, and are clearly set forth in the *Statistics of the Saginaw Valley* for 1868:

> The operations of this company have been completely satisfactory, and the organization is unquestionably of great benefit to the salt manufacturers who have availed themselves of the advantages it offers. It has, so far as its line of operations has extended, brought about the one thing needful, a uniform system of inspection, and introduced system, order and reliability into a business, which, without such general regulations, has in no quarter ever proved remunerative.

In spite of the competition of New York and the Ohio river (relieved in part by an agreement with the Onondaga Salt Com-

pany which will be considered later), the business grew with remarkable rapidity, and the association ran smoothly till 1871, when the vigorous efforts of some of the members opposed to the management became of serious moment. The real merits of the controversy, which became bitterly personal, several letters of a violently abusive character being published, it is hard to determine. On the one side, charges of mismanagement, even of dishonest practices, were made against the officers of the association by Duncan Stewart, president of a salt manufacturing company; on the other, Stewart's dissatisfaction was said to have been caused by the refusal of the managers to ship salt by a line of boats in which he was interested, at rates above those offered them elsewhere. For our purpose it is enough to know the result. In the *Annual Statement* of the business of the Saginaw valley for 1871, we find it in compact form:

> In salt, the season of '71 may be quoted as of extra activity both in manufacture and sale. Early in the season it became evident that a commercial rivalry had been excited which could not end but by the going to the wall of one of the parties engaged in it. Assuming the shape of individual antagonism to a corporate company, it became at an early day evident that many of the manufacturers who are members of the Salt association, would take sides with the opponents of the association, and as a result fully one-fifth of the entire salt product of the valley, which under ordinary circumstances would have been handled by the association, was purchased by the firm of J. L. Hurd & Co., of Detroit, at prices in advance of those realized by those who remained in the association. Since the close of navigation, the association has resolved to suspend operations for the present, and each manufacturer will, during the season, be left free to realize as best he may on his products.

It is significant, and somewhat surprising to note that by the determined efforts of one man, the association was forced to suspend operations, even though, as has been reported, this man was compelled to destroy his own financial standing to bring about such a result. Table I, again, furnishes us with an interesting comment upon this financial battle. For 1872 the production of salt in the state is more than 3600 barrels less than that of the year preceding; whereas both 1871 and 1873 show a gain of about 100,000 barrels.

Five years passed before a thoroughly effective union could again be made. Smaller organizations were formed to sell salt for groups of manufacturers, notably the Saginaw Salt Association and the Michigan Salt Association; but the competition was fierce, prices went steadily down, and the weaker companies found themselves in need. At length, after low and declining prices throughout the year 1875, the time seemed ripe for another organization which could control the sale of a large proportion of the Michigan salt, and through this added power of union both secure a saving in the expenses of sale and transportation, and either compete more effectively with the New York and Ohio river manufacturers or force them into a union which should control the whole American product. January 8, 1876, J. E. Shaw, president of the Michigan Salt Association (a smaller combination of manufacturers), issued a circular address to the salt manufacturers of Michigan, calling a meeting to be held at Bay City, January 20, to effect such an organization, if it should be possible. The address exhibits in an almost pitiable light the situation of the manufacturers, and urges strongly the need of organization. Mr. Shaw declared:

The old adage, "in union there is strength," is true wherever you apply it, and in manufacture of salt there is no exception. To secure this *union* with its attendant *strength* is the object of the Michigan association. This is the object it had in view when it was organized, and this is the object it has in view to-day. That the organization has remained inactive, is attributable to the fact that it could not secure control of a sufficiently large *percentage* of the state product to warrant [aggressive action], a few manufacturers declining, for reasons best known to themselves, to enter the association. And what was the result? Salt has depreciated in value, dropped steadily down, until to-day it has no market price on the Saginaw river, and is quoted at only $1.27 in Chicago, and $1.00 in Toledo. That the experience of '75 will be that of each succeeding year, unless something is done to check the general demoralization, cannot be gainsaid. The oldest manufacturers of the Syracuse, Kanawha, and Ohio districts, tell us that their experience, dating back forty years in some cases, has *always* been this: "*Organized we have prospered. Unorganized we have not.*" This is the experience which we have been buying and paying dearly for. . . . The trouble lies in the *marketing* of the product. Each man has taken care of (or

attempted to) his own product. . . . The other salt districts of the United States are now organized, and are ready to treat with us (as soon as we have an association) relative to fixing and maintaining prices, dividing the territory, and making other arrangements which will inure to the advantage of the trade. But we must first be organized. They cannot treat with individuals.

The appeal was successful. The meeting was held; others followed; and in April the Saginaw Salt Company and the Michigan Salt Association were consolidated and other outside firms were taken in, so that from the beginning more than 85 per cent of the product of the state was controlled. The new association took the name of The Michigan Salt Association.

When in 1881 the association expired by limitation, it was immediately reorganized under the name of The Salt Association of Michigan; and, in 1886, again expiring by limitation, it was again organized under its former name. The three associations have been, in fact, the same association under different names; the president and secretary elected in 1876 still hold their offices, and the business is conducted on the same principles, slight changes only having been made in the articles of association and by-laws.

The organization of the association, effective as it is, is very simple. Less than a page contains the articles of association, which declare that the purpose of the association is "the manufacture and dealing in salt," and the "transportation of its products to market"; that the amount of capital stock shall be $200,000, divided into $25 shares, of which the amount actually paid in is two dollars per share; that its affairs shall be managed by a board of nineteen directors (of whom not more than one shall be from the same firm or company of manufacturers) chosen by the stockholders; that the offices for transaction of business shall be in East Saginaw and Bay City, and that the business shall be carried on in the salt-manufacturing counties; and, finally, that the association shall exist as a corporation for the period of five years.

From the by-laws, we learn that the stockholders shall be manufacturers of salt, and that the number of shares taken by any one "shall not exceed one share of the capital stock for

every barrel of the average daily capacity of his manufactory on a fair estimate" — an excellent provision to prevent manipulation of stock to the detriment of the real business.

An annual dividend of seven per cent payable semi-annually on the amount of stock actually paid in, together with the losses, costs and expenses incurred in handling and selling, including the state inspection fees, is deducted from the proceeds of sales before division is made.

That the business management of the association may be as personal and direct as possible, the president is given the general supervision of the entire business, subject to the general rules laid down by the board and the executive committee. A secretary and a treasurer with the usual duties of such officers are appointed by the board, and also an executive committee, which has general control and is charged with the duty of auditing all accounts, inspecting all books, etc., at least once a month. The officers receive a stipulated salary. The organization, it will be seen, is such that the executive efficiency of a single head is combined with all proper checks to guard against any abuse of trust on the part of any of the officers. The fact that the chief officers of the association have held their positions since its organization, and the continued prosperity of the association, never greater than now, reflect the greatest credit on the management as well as on the authors of the plan.

The relations of the association with the members, however, constitute the main point of interest. A contract is made *every year* with each manufacturer who wishes to become a member, in accordance with Article vii of the by-laws, which reads as follows:

> Every manufacturer, in becoming a member of this association, shall execute and deliver to it a contract for all salt manufactured by him or them, or a lease of his salt-manufacturing property, including all apparatus and appurtenances thereunto belonging, for the purpose of manufacturing. Such contract or lease shall be for the term of one year, or until the dissolution of the association, and shall not impose any restriction that will prevent the manufacture of salt at any and all times.
>
> Each and every contractor shall manufacture salt for this association on the terms and conditions as follows:

That he will make salt solely on the association's account, of the best quality of the kind manufactured by him, according to the conditions of his contract or lease.

The contracts provide, further, that in case the manufacturer sells salt on private account, he shall pay to the association ten cents for every barrel so sold; that the contract, however, is not thereby forfeited, but remains in force throughout the stipulated time.

While this gives full control of the product to the association, and effectually prevents all competition among the manufacturers, the provision that no restriction shall be imposed which will prevent the manufacture of salt at any and all times, operates powerfully against any raising of prices to exorbitant rates such as might perhaps be secured otherwise, if combination with the New York and Ohio river manufacturers could be effected. The reason that this clause stands in the by-laws, and that the practice of the association differs so entirely, on this point, from that of the anthracite coal syndicate and other combinations of like character, is found in the peculiarity of the manufacture. A great part of the larger salt blocks are run in connection with saw-mills; and the slabs, sawdust, etc., from the mills are used for barrels and fuel. Not only would this material, if not so used, be a dead loss, but its removal would be a source of expense. Manufacturers so situated could never expect a rise in the price of salt sufficient to compensate them for the loss that would be incurred in stopping their works; and consequently they will not join the association unless assured that they will not be subjected to such a loss and inconvenience in their more important business.

Another provision of great advantage, especially to the manufacturer of comparatively small capital, is that which provides for an advance of money on all the salt inspected each month, whether the salt is taken from the bins and sold or not, if the manufacturer wishes such advance and is willing to pay interest on it. The rate of advance and the rate of interest are fixed by the board and may be changed from time to time; but liberality is always shown both in the amount advanced and in the rate of

interest. The advance has been lately 25 cents per barrel in the bins, or 45 cents per barrel if packed, with interest at 7 per cent. Money may be loaned in the state at 10 per cent, and this rate is often obtained on small sums for short periods of time.

The salt becomes the property of the association as soon as inspected; but the manufacturer is still bound to deliver it free of charge on the wharf or on the cars, as the association shall direct, and to sustain all losses by fire or otherwise, if they occur before such delivery. The association agrees on its part to remove within a reasonable time all the salt manufactured.

Reports are rendered every month to each member of the association, giving not merely his own special account, but all the sales, with the average price both gross and net, and all the necessary expenses with principal items — average freight, commission, home and storage charges, etc. All the members receive credit at the same average rate, and for an amount proportioned to their manufacture as shown by the inspection — a provision greatly to the advantage of the poorly situated companies. The receipts of salt for each month are sold and accounted for separately.

The association keeps its agents — most of them selling on commission, but some on salaries — in Chicago, St. Louis, Cincinnati, Cleveland, Columbus, Duluth, Detroit, Milwaukee and other places, wherever this is warranted by the amount taken.

It will perhaps be well, further, to notice some attempts that have been made, since the manufacture of salt in Michigan became a leading industry, to form combinations of all the leading manufacturers in the country, and thereby to secure from consumers a price limited only by the competition of foreign salt and the lessened demand consequent on the rise in price.

Not many months after the Saginaw and Bay association was formed (April, 1868), the managers began negotiations with the manufacturers in New York and in the Ohio river district. This first attempt, instead of resulting as had been hoped, led, from a rather peculiar combination of circumstances, to an even fiercer competition than had existed before.

The president of the association gives the facts in his report of 1870 to the board of directors. The association in Michigan

succeeded in making terms with the Onondaga Salt Company, but failed with the Ohio river association, because the latter could not control the product of their district either as to quantity or price. Some new works at Pomeroy, it seemed, had refused to join the Ohio river association. The other manufacturers of that district, having sold *all their product* to the association *at a fixed price*, increased their output and flooded the market. As the association could not control the works at Pomeroy, there was a general cutting of prices in which, of course, Michigan and New York were compelled to join. As the eloquent writer puts it: "It was a Donnybrook Fair in the salt market. When you saw a head, you hit it." The immediate result was, naturally, detrimental to all the works. The final outcome was that the outsiders on the Ohio river joined the association, and a change in the character of the contract with the former members enabled that association to control the *quantity* as well as the price in that quarter. This being done, it became an easy matter to make the combination general. The Washington correspondent of *The Chicago Tribune* gave an account of the pool which is corroborated by other papers and by officers of the present Michigan association. The Syracuse, the Ohio, and the Saginaw and Bay companies entered into an agreement at Detroit, March 22, 1871,

> To make a pool of all the salt in the market in the territory bounded by the lakes on the North and East and by the Ohio river on the South, the western and southwestern boundary to be entirely discretionary, according to the prices of freights to places whence orders for this article might be sent. This discretion was confided in a board, there appointed, which consisted of one representative from each of the three salt corporations, who are also empowered to fill orders and forward all supplies, to advance or reduce prices as occasion may require. The percentage of the pool, and all future supplies and profits under existing arrangements, were agreed to as follows: Syracuse, 40 per cent; Ohio river, 32 per cent; Saginaw, 28 per cent.[1]

The prices fixed were $2.00 per barrel for Chicago, Cincinnati, Cleveland and Detroit; $2.10 for Toledo; and $2.40 for St. Louis.

[1] *The Chicago Tribune*, April 4, 1871.

Reference to Table II (see page 15) will show the effect of the "Donnybrook Fair" period, as well as the rise in price consequent on the pool in 1871. The Chicago prices of the first of January show the effects of both movements, as do also the average prices at Saginaw. Gold prices show a less decrease, but emphasize the rise in 1871–2. At the close of 1871, as we have seen, the Saginaw and Bay association, having lost control of a large proportion of the Michigan men, could not uphold their end of the bargain. As they were not bound, however, to take *at a fixed price* any large product, no such immediate cutting of prices followed as had been seen the year before.

A somewhat more firmly controlled pool was made ten years later to cover about the same territory. A special arrangement was made with the Ohio river manufacturers, the exact terms of which cannot be given; but they are of little consequence, since by far the larger part of the amount was sold by the other companies.

The territory covered was bounded on the east by a line drawn north and south through Buffalo, and on the south by the Ohio river, as before. The importance of the Michigan product, relatively speaking, is worthy of special notice. In 1871, as we have seen, Michigan put in 28 per cent; Ohio river, 32 per cent; and New York, 40 per cent. In 1881, Michigan put in $\frac{15}{17}$ and New York $\frac{2}{17}$, while some special arrangement regarding a small fixed number of barrels, or a fixed rate, was made with the Ohio company. The management of the pool, as before, was confided to a committee selected from both companies. The contract went into effect May 1, 1881, and was terminated March 1, 1882, a month's notice having been given by the Michigan association in accordance with the terms of the contract. The effect of the pool on prices is shown in Table III (page 16). The cause for the breaking of the pool, and the following sudden lowering of prices, is stated by the managers of the association to be simply that the markets, especially Chicago, had become overstocked with salt, and the Michigan association felt the need of having full control there. They broke the pool, and "slaughtered the market."

Though other combinations have been talked of at times, no other has been made.

Such, in brief, is the history and the plan of organization of The Michigan Salt Association. It remains to consider somewhat more fully its economic effects.

First, much credit must be given the association for the improvement of the quality of the salt manufactured in the state. The necessity for a rigid system of inspection to keep up the quality of the product and prevent injury to the reputation of Saginaw salt in the market, led the old Saginaw and Bay Salt association to appoint a committee in 1868 to draft a law meeting the wants of the salt manufacturers. As early as 1865 a system of local inspection had been adopted by a number of manufacturers,[1] but something more rigid was required; and this bill, which became a law in March, 1869, was the result. As amended in 1875, it remains to-day in the statute book, and to it is doubtless due in large measure the superior quality of the Michigan salt.

The inspector is appointed by the governor and senate, is paid a stated salary by the state, and is, of course, entirely independent of the manufacturers. The state is divided into as many districts as seem to him practicable for the thorough carrying-out of the work, and all salt made is carefully inspected, a deputy inspector visiting each block *every day* for this purpose. The early association deserves the credit of securing this effective law. Some manufacturers, it is true, attempt at times to evade the law and to pass off an inferior grade of salt for the best; but the larger manufacturers, and of course the Salt association, are interested in having the grade of salt kept up, and therefore assist the work of inspection as much as possible.

The question which next suggests itself — that of the influence of the association upon prices and profits — cannot be answered so briefly. In many of the markets it is clear that the association is really without competition as long as it keeps its prices reasonably low, or perhaps we had better say, only moderately high. The effective competition of New York — or even that of any Michigan manufacturers who are "running

[1] S. S. Garrigues, Saline Interests of Michigan, p. 32.

wild" — is practically out of the question. It must not be forgotten that the average cost of manufacture in Michigan is considerably less than in New York; and though westward-bound freights are low, they are still worthy of consideration. Of course no single manufacturer could escape competition to so great an extent, since his neighbors would be his strongest competitors. Again, by means of its thorough organization and the daily reports sent to the home office by agents in all important markets, the association is able to make sales not merely more advantageously as regards price, but also with a much less expense in the way of commissions, travel, number of agents, etc. Besides this, the freedom from care and responsibility and the certainty that the product is in hands that will make the most of it, is worth not a little to the average manufacturer. The last-named item alone, that of greater intelligence and knowledge of the market, should receive more consideration than the manufacturer usually gives it.

Another point of advantage is this: by means of its large sales and long experience, the association can reduce losses from bad debts to a lower figure than could individual manufacturers.

Further, when the sales are all made from a central point, with a right to deliver from any of the manufactories at will, it is clear that a large saving in transportation can be made. Contracts will be filled always from the works most favorably situated. Vessels and cars can be secured at such times and places as will enable them to carry at the lowest rates. The average rate of freight is thereby much lessened.

The plan of advancing a large part of the value of the salt to the manufacturer before the salt is sold, enables him to carry on his business with less capital than would be required if he were not a member of the association.

The first consideration, the abolition of competition, comes solely to the benefit of the manufacturer; the others mentioned are advantages from organization which lessen the cost of production, — including sales and transportation, — and may benefit either the manufacturer, through greater profits, or the consumer, through lower prices, or the benefit may be divided.

A study of prices before the formation of the association, and

after, would seem to show that while the saving had chiefly benefited the manufacturer, as was to be expected, the consumer had not suffered seriously.

TABLE II

PRICE OF SALT PER BARREL IN SAGINAW AND CHICAGO

YEAR	SAGINAW	CHICAGO
1860, January 1,		$1.50
1861, Jan. 1,		1.75 @ 2.00
1862, Jan. 1,		2.25
1863, Jan. 1,		2.25
1864, Jan. 1,		2.10 @ 2.15
1865, Jan. 1,		2.75
1866, Jan. 1,		2.35 @ 2.40
1866, average,	$1.80	
1867, Jan. 1,		2.40 @ 2.45
1867, average,	1.77	
1868, Jan. 1,		3.25
1868, average,	1.85	
1869, Jan. 1,		2.60
1869, average,	1.58	
1870, Jan. 1,		2.25 @ 2.30
1870, average,	1.32	
1871, Jan. 1,		2.05 @ 2.10
1871, average,	1.46	
1872, Jan. 1,		2.35 @ 2.40
1872, average,	1.46	
1873, Jan. 1,		2.40
1873, average,	1.37	
1874, Jan. 1,		1.90
1874, average,	1.19	
1875, Jan. 1,		1.65
1875, average,	$1.10	
1876, Jan. 1,		$1.35
1876, average,	1.05	
1877, Jan. 1,		1.40
1877, average,	.85	
1878, Jan. 1,		1.10
1878, average,	.84	
1879, Jan. 1,		1.10
1879, average,	1.02	
1880, Jan. 1,		1.45
1880, average,	.75	
1881, Jan. 1,		1.05
1881, average,	.83⅔	
1882, Jan. 1,		1.35
1882, average,	.70	
1883, Jan. 1,		1.00
1883, average,	.81	
1884, Jan. 1,		1.15
1884, average,	.75⅔	
1885, Jan. 1,		.95
1885, average,	.70	
1886, Jan. 1,		.95
1886, average,	.66	
1887, Jan. 1,		.80
1887, average,	.57½	

Table II shows that, while the prices have on the whole tended downward since 1876, the time of the formation of the association, the rate of decrease has been somewhat less rapid. On the other hand it must be noted that the prices in the earlier years are reckoned in legal tender notes. This causes the prices during the sixties, and the rate of decrease during the years preceding resumption, to appear greater than they really were, though a slight check in the rate of decrease can be seen even when prices are reckoned in gold. The influence of the war, too, in pushing the price to what was really an abnormal height, must not be overlooked. The improved methods of manufac-

ture would naturally cause a lowering of price, and it is impossible to accurately judge the influence of all the factors. The earlier prices, of course, were not determined to any marked extent by the Michigan product, as the manufacture in the state began in 1860, and was not really on an even footing with New York for several years. It seems probable, however, that the association checked somewhat the tendency toward a lower price, and, if so, the consumer is so much the worse off. This difference in price cannot on the whole have been much, the chief advantage to the manufacturer coming, probably, from the lessened cost of putting his product on the market.

It is, again, quite probable that without the association, the larger dealers would take part of the profit which now goes to the manufacturer, and that the consumer would be forced to pay as much as now, and even more. Certain it is that large dealers in Chicago, Toledo, Cleveland and Sandusky express themselves generally as opposed to any association, even when they have been appointed agents. At present they receive a low commission per barrel of salt sold; whereas, before the formation of the association, they could buy salt in the summer months when it was very plentiful, and store it till after the close of navigation, and then the few larger dealers in such an important market as Chicago, by uniting, could advance the price enough to reap a handsome profit. This practice, which was common, came to the benefit of the few dealers, while neither the manufacturer nor the consumer received any share.

TABLE III

Association Price of Salt each Month, from June, 1877, to November, 1887[1]

June 1877	$0.80¼	Feb. 1878	.70	Oct. 1878	.70
July "	.79	March "	.71	Nov. "	.70
Aug. "	.72½	April "	.76	Dec. "	.70
Sept. "	.74½	May "	.75	Jan. 1879	.72
Oct. "	.74	June "	.77	Feb. "	.80
Nov. "	.75	July "	.77	March "	.83
Dec. "	.80	Aug. "	.76	April "	.82
Jan. 1878	.73	Sept. "	.70	May "	.80

[1] Prices given are for the sales of the preceding month.

TABLE III — *Continued*

Month	Price	Month	Price	Month	Price
June 1879	.80	April 1882	.71	Feb. 1885	.69
July “	.86	May “	.72	March “	.68
Aug. “	.88	June “	.70	April “	.66
Sept. “	.90	July “	.70	May “	.63
Oct. “	.94	Aug. “	.70	June “	.62
Nov. “	1.02	Sept. “	.69	July “	.60
Dec. “	1.05	Oct. “	.69	Aug. “	.60
Jan. 1880	1.05	Nov. “	.69	Sept. “	.65
Feb. “	1.08	Dec. “	.70	Oct. “	.70
March “	1.09	Jan. 1883	.70	Nov. “	.72
April “	1.05	Feb. “	.70	Dec. “	.73
May “	.85	March “	.70	Jan. 1886	.71
June “	.72	April “	.70	Feb. “	.72
July “	.72	May “	.75	March “	.71
Aug. “	.72	June “	.80	April “	.70
Sept. “	.72	July “	.80	May “	.69
Oct. “	.72	Aug. “	.80	June “	.68
Nov. “	.72	Sept. “	.80	July “	.66
Dec. “	.72	Oct. “	.81	Aug. “	.65
Jan. 1881	.74	Nov. “	.83	Sept. “	.65
Feb. “	.77	Dec. “	.83	Oct. “	.63
March “	.77	Jan. 1884	.83	Nov. “	.60
April “	.76	Feb. “	.83	Dec. “	.60
May “	.76	March “	.83	Jan. 1887	.60
June “	.76½	April “	.83	Feb. “	.60
July “	.81½	May “	.80	March “	.57
Aug. “	.88⅛	June “	.74	April “	.55
Sept. “	.92½	July “	.72	May “	.55
Oct. “	.94	Aug. “	.71	June “	.53
Nov. “	.95	Sept. “	.70	July “	.51
Dec. “	.95	Oct. “	.70	Aug. “	.57
Jan. 1882	.94	Nov. “	.70	Sept. “	.58
Feb. “	.99	Dec. “	.69	Oct. “	.60
March “	.99	Jan. 1885	.68	Nov. “	.62

Table III, giving the average monthly prices of the association (the net prices paid to manufacturers), shows, on the whole, a decline; but one not so great after all, when one considers the general tendency of prices of all manufactured products. Moreover, there are several times when the price has gone up enough to counterbalance in great part the decline.

Besides the statements of reliable manufacturers regarding their profits, a comparison of the table of prices with the table showing the amount produced in different years in Michigan

gives us still further reason for the belief that the association cannot secure prices which make the profits at all extraordinary. A distinctly marked rate of increase (not absolute increase) or falling off in production usually follows, especially in later years, like changes in the average yearly price. One should not lay too much stress, however, upon such similarities, as there are many other determining factors.

Many of the advantages to manufacturers of such an association, especially the freedom from competition with one's neighbors, cannot be secured unless a very large proportion of the manufacturers of the state are united. The association aims, of course, to have as many join as possible; and in case of necessity it does not hesitate to "squeeze" a manufacturer whose block is so situated that he has no need of the association, and whose competition is troublesome. This brings to our notice the disadvantage it might be to some manufacturers to become members. As the prices, freight charges, etc., are arranged for the whole association, the manufacturer who has a ready market near at hand could oftentimes realize somewhat more by remaining outside.

In the year 1886, about 600,000 barrels of Michigan salt were sold by outsiders. The amount was large enough to make a real competition that could be severely felt by the association. At length, the managers issued the order to their agents to meet any rates, however low they might run. Table III shows the gradual decrease, as the fight went on. In August, 1887, the unprecedentedly low price of 50 cents per barrel was reached. In the same month manufacturers representing some 350,000 to 400,000 barrels, yearly product, joined the association; and we note the consequence in the rise of price to 57 cents for that month's product, while the prices for the following three months (58, 60, and 62 cents) still show the upward tendency.

It has been impossible to obtain with any degree of accuracy the data which would indicate the influence of the competition within the state; namely, the times of the accession of different manufacturers to the association and of their withdrawal from it. As the contracts are made yearly, some enter the association

and others leave it every year. In one or two instances, however, the effect of such changes is marked. Reference to Table III shows, in 1880, a sudden decline in price from $1.09 to 72 cents within three months. This is probably to be explained by the fact that "a large number of the manufacturers went out March 1, and that they commenced cutting prices, and we [the association] concluded to more than meet them." [1] The sudden drop in prices in the early part of 1882 followed the breaking of the pool with New York. The rise in August, 1887, is due, as noted above, to the accession of a number of manufacturers. It should rather be called the setting back of the price toward that obtained before the cutting to force the manufacturers in. Doubtless, too, many of the other changes noticed are to be ascribed to the same causes.

When a barrel containing 280 lbs. of fine salt of the first quality can be bought in the Chicago market at a price ranging from 75 to 85 cents, there is not likely to be very much complaint on the part of consumers, nor much talk about "monopolies," "coalitions for robbing the people," etc.; and yet the Michigan Salt Association is sometimes attacked as a monopoly, and it doubtless has some of the features of one. Adolph Wagner is strongly inclined to recommend the manufacture of salt by the state, on account of the danger of so common an article of consumption being monopolized by the manufacturers and dealers.[2] The advisability of state control seems to him, on the whole, greater than in the case of the coal industry. Our experience with anthracite coal companies within the past few years has been such that we may well note the circumstances of our salt industry in this regard. Is it likely or even possible that a really oppressive monopoly in this article can be made?

The salt-producing territory of the United States, while widespread, is nevertheless so limited that competition in manufacture is by no means so free as in other lines where the raw material may be shipped in at low rates; *e.g.* cotton, or shoes. This makes it much easier for two or three combinations to unite

[1] Letter from the secretary of the association.

[2] Wagner, Finanzwissenschaft, Bd. I, §§ 251, 254.

and control the whole product; and we have seen that in two instances, at least, for short times, such a union was made to control "disputed territory" — an expression, by the way, which in itself emphasizes the limited nature of the competition.

The coal and petroleum industries have been able to secure complete control by the aid of the railways. Aside from the fact that the capital invested in salt is much smaller, it would be much more difficult for the associations to control the means of transportation. The territory is more widely scattered, and is, besides, much of it adjacent to the great lakes. Such a control as the coal syndicates exercise, would require a controlling influence over all the larger railways east of the Mississippi, and over the boats on lakes Huron, Michigan and Erie, as well.

A further matter to be noted is the large import of salt. In 1880 some 38 per cent of all the salt used in the United States came from abroad. Though part of this is of a different quality and does not enter into competition with the American product, yet a large part of the sea-board traffic in salt, and the larger part of the salt used in the South, is controlled by the importers. The salt is brought as ballast, so that the cost of transportation to our coast is practically nothing. It is the cost of transportation from the sea-board that keeps it out of the territory now controlled by the Michigan association. It may be readily seen that our protective tariff on salt would need to be far higher than at present, before our manufacturers, even if all in the United States were united, could command prices comparable, when considered with reference to the cost of production, to those obtained on anthracite coal. The character of the combinations, too, would need to be much stricter.

Without such combinations, considering the Michigan association as it is, the New York competition is enough to keep the price from becoming exorbitant. Add to this the above-mentioned fact that the association has no power to limit production, and the fact that new wells are being sunk continually, whose owners can be forced to join the association, if inclined to remain outside, only by a tedious and expensive fight on prices, and the dangers to consumers from the association seem slight. Doubtless, the manufacturers who have been in effect

forced into it, and who feel that without an association in the state more profit could be made, are inclined to think that such a combination is oppressive. These manufacturers, however, form but a small proportion of those in the state.

The conclusion to which one must come, then, regarding the influence of the association is this: it is probable that the average consumer is but slightly affected, though it is possible that he has to pay a little more for his salt than would otherwise be the case; it is certain that, with the exception of a few who are uncommonly well situated, the manufacturers are decidedly benefited by the association. Certain it is that most of them are well content, and that the association never stood firmer than it does to-day.

J. W. JENKS

The subsequent history of combination in this industry has been unfortunate. The National Salt Company was organized in New Jersey in 1899, acquiring the business of a company of the same name chartered by West Virginia. Most of its properties were in New York, but the company purchased the best plants in Ohio and Michigan, claiming in 1900 to include 94 per cent of the evaporated salt of the entire country excepting the Pacific coast. In 1900 plans for controlling salt works in Spain and Italy were inaugurated.

The next step was the formation of a New Jersey company in 1901, known as the International Salt Company, which absorbed the National by interchange of securities. This operation was financially tainted by the enormous compensation, amounting to about one third of the stock of the new company, issued to the promoters. By 1902 also it became clear that the National Salt Company, which had been paying dividends at 8 per cent on the common stock, was practically insolvent, not even having earned interest on its bonds. It was officially stated that this embarrassment was due more to extravagant purchases of plants than to losses in operation. Meanwhile disorganization and losses of property under receivership has greatly reduced the proportion of the entire industry controlled. In so far as the possession of natural salt deposits constitutes a basis for monopoly, a foundation for successful combination would seem to be present; but failure has evidently resulted hitherto from a combination of extravagance, mismanagement and perhaps even downright fraud. — ED.

NOTE. The admirable account of the later salt combinations in A. S. Dewing. Corporate Promotions and Reorganizations, Harvard Economic Studies, 1914, chapter VIII, brings experience down to date.

II

THE DEVELOPMENT OF THE WHISKEY TRUST[1]

IT is probably too soon to tell with even a reasonable degree of certainty what the outcome of the present tendency towards combination among producers is to be. So far there have been not a few egregious failures, the most noteworthy being the collapse of the copper syndicate — though that was hardly a trust, technically speaking; but there have been also a few apparently noteworthy successes. It seems clear, at any rate, that we have still some time to wait before we can say what the resulting normal is to be; and in the meantime it seems best not to be too hasty in exterminatory legislation, in sweeping denunciation nor in unqualified praise, but to study as accurately as is possible the history, management and tendency of the individual organizations, that when the time for action comes we may act with knowledge. The present article is an attempt to describe, as accurately and fully as the information that can be secured will permit, one of the (apparently, at least) most successful of these organizations: "The Whiskey Trust"; more accurately: "The Distillers' and Cattle-Feeders' Trust." The significance and tendency of such an organization as this cannot be understood without a knowledge of the circumstances leading to its formation. In this case, interest is added by the fact that legislation by the United States and by some European nations is, doubtless, indirectly responsible in good part for the condition of business that led to the formation of the trust.

It is well known that, from the establishment of our government till the outbreak of the Civil war, distilled spirits were for the most part comparatively free from taxation by the United States. The tax levied by the recommendation of Alexander

[1] Abridged from the *Political Science Quarterly*, Vol. IV, 1889, pp. 296–319. For additional references, see footnote on p. 45 *infra*.

Hamilton, which led to the Whiskey insurrection in Western Pennsylvania, was comparatively very light (only 9 to 11 cents per proof gallon, as compared with 90 cents at present), and even this was repealed soon after the accession of Jefferson to the presidency. From that time, with the exception of four years (from 1813, when an increase of revenue was necessary to carry on the war, till 1817), spirits were free until the outbreak of the Rebellion. As a consequence, they were sold at a very low price, — 24 cents on the average in New York for the five years preceding 1862, with a minimum price of 14 cents per proof gallon, — and there was little temptation to overproduction for either the home or foreign market.

At the outbreak of the Rebellion the necessity for increased revenue that led to the imposition of internal taxes wherever it was thought that a revenue could be raised, "without much regard to acknowledged politico-economic laws or precedents,"[1] resulted, of course very properly, in the taxation of distilled spirits. The first tax of 20 cents a proof gallon (July 1, 1862) was followed, March 7, 1864, by an act raising the tax to 60 cents per gallon. July 1 of the same year the rate went to $1.50; and January 1, 1865, to $2.00 per gallon.

At each increase of the tax, considerable time intervened before the highest rate was imposed. As a natural consequence, distilleries were run to their utmost capacity, and even new distilleries were built to get a stock on hand.[2] As Mr. H. B. Miller, the president of the whiskey pools, writes:

> Some time intervened before the various amounts were collected, and during this time the distiller and speculator had nearly the whole benefit of the tax without paying it. The speculation in whiskey during this time was tremendous. Editors, ministers, statesmen, — all took a hand. Distilleries were erected all over the country, and at the end of the war there was three times the capacity that could be utilized.

[1] Reports of United States Revenue Commission, 1865–66, p. 2.

[2] *Ibid.* p. 6: "Thus, for example, the commission estimate that on the 1st of July, 1864, the date when the advance in the tax on distilled spirits of from 60 cents to $1.50 per gallon took effect, there *were made and stored*, in anticipation of this advance, at least forty millions of gallons, or a quantity sufficient to supply the wants of the country for at least a year in advance."

To the same effect David A. Wells, in the article on "Distilled Spirits" in Lalor's *Cyclopedia of Political Science*, writes:

> The immediate effect of the enactment of the first three and successive rates of excise was to cause an almost entire suspension of the business of distilling, which was resumed again with great activity as soon as an advance in the rate of tax in each instance became probable. The stock of whiskey and high wines accumulated in the country under this course of procedure was without precedent; and Congress, by its refusal to make the advance in taxation, in any instance, retroactive, virtually legislated for the benefit of distillers and speculators rather than for the treasury and the government. The profits realized by the holders of stocks, thus made in anticipation of the advance in taxation, has probably no parallel in the history of any similar speculation or commercial transactions in this country, and cannot be estimated at less than $50,000,000.

When the period of speculation was over, the great amount of surplus capacity for manufacture and the large amounts of stored products on hand made it, of course, almost or quite impossible for distillers who did not practise frauds on the revenue to continue in business. The high taxes, however, led to such frauds that whiskey often sold in the market for less than the amount of the tax.

Another factor that contributed to the general depression was the lessened demand for alcohol for use in the arts and manufacture. With alcohol at 30 or 40 cents a gallon, it was used in large quantities for the manufacture of burning fluid, varnishes, furniture polish, perfumeries, patent medicines, even as fuel for cooking, etc.; the United States revenue commission estimating that in 1860 not less than 25,000,000 gallons of proof spirits were so used. When the tax was $1.50 and $2.00, or even 50 cents, as it was from 1868 to 1872, spirits, of course, became too expensive for such purposes. As the tax has been still higher since that date (70 cents till 1875, and 90 cents since that time), no increased demand for such purposes has been felt.

These causes, including the large amounts fraudulently manufactured in the earlier years of the high taxes, had tended to

keep the distilling business in a comparatively depressed condition after the speculative period following the war had passed. Even as early as 1870 or 1871 the distillers felt themselves compelled to enter into an agreement to limit their distilleries to two-fifths production; and all north of the Ohio, with two or three exceptions, made such an agreement. No very decisive effect, however, was produced by this arrangement. The facilities for manufacturing adapted themselves gradually to the demand; and, on account of our cheap grain, a fair export trade was growing up that relieved the situation somewhat. But in the years from 1878 to 1882, on account of successive crop failures in Europe, a very heavy export demand at paying prices sprang up. In 1879, 1880, and 1881, nearly 16,000,000 gallons a year were exported.

TABLE I

SPIRITS REMOVED IN BOND FOR EXPORT[1]

Year	Taxable (proof) gallons exported	Percentage of production	Year	Taxable (proof) gallons exported	Percentage of production
1873 . . .	2,358,630	3.45+	1881 . . .	15,921,482	13.52+
1874 . . .	4,060,160	5.90+	1882 . . .	8,092,725	7.64+
1875 . . .	587,413	0.96+	1883 . . .	5,326,427	7.19+
1876 . . .	1,308,900	2.25+	1884 . . .	9,586,738	12.70+
1877 . . .	2,529,528	4.22+	1885 . . .	10,671,118	14.24+
1878 . . .	5,499,252	9.80+	1886 . . .	5,646,656	7.02+
1879 . . .	14,837,581	20.63+	1887 . . .	2,223,913	2.85+
1880 . . .	16,765,666	18.55+	1888 . . .	1,514,205	2.15+

To meet this demand many new distilleries, including some of the largest in the country, were built, while the old ones, of course, were run at full capacity. After 1880, good crops in Europe, poor crops at home, with some changes in the tariff laws[2] of leading European countries, especially discriminating duties against the United States, cut off this demand, and left

[1] Report of the Commissioner of Internal Revenue, 1888.
[2] René Stourm, L'Impot sur l'alcool dans les principaux pays, p. 48.

the distilleries of this country with a capacity sufficient to produce four times what the home market needed.[1]

Of course, there was, at first, great over-production, and consequent distress among distillers. They could not export except at a loss; their cattle were in the barns (the feeding of cattle on the slop from the distilleries is one important adjunct to the distilling business), so that it was difficult to close the distilleries; their warehouses were filled with goods, and the market was broken. Something must be done.

Some said: Let this go on and let the fittest survive. Our experience was that a distiller would keep on until all his own money and all he could borrow was gone, and when he was used up there was another man ready to step in his shoes.[2]

In November, 1881, a general meeting was called to form a pool. Prices were really below the cost of manufacture in many places, and the only remedy seemed to be to limit the output, and to export the surplus, even at losing prices. The "Western Export Association" was formed, the officers of which were authorized to levy a monthly assessment on each distiller running his distillery. This assessment was to be proportionate to the amount of grain used in manufacture, and high enough to pay the losses arising from the exportation of a quantity of spirits sufficient to relieve the home market.

An appeal was made to Congress, asking that an export bounty be given equal to that granted by Germany; or, if a bounty for export should not be given for fear of lessening the revenue, that the internal revenue tax be raised to $1.00 and then a bounty of 10 cents for export be granted. Congress and

[1] In the references to the trade, especially the exports, all the manufacturers of whiskey have so far been considered. As the whiskey pools have mostly concerned only one branch of the business, and as the trust is limited to this branch, *i.e.* the manufacturers of a product for immediate use, it is worth while to call attention to the distinction. One class of producers, especially those in Kentucky, manufacture "Kentucky whiskey," technically so called, *i.e.* a product that needs to be stored for some time (from two to five or more years) before it is in good condition for use (J. M. Atherton: Testimony before Committee on Manufacture, p. 3); the other class of distillers, located mostly north of the Ohio river, manufacture alcohol, pure neutral or cologne spirits, etc., a product that is fit for immediate use.

[2] Letter from H. B. Miller, former president of the pool.

the people, however, had not forgotten the whiskey-ring scandal, and consequently Congress did not dare legislate in favor of distillers, even if such legislation should injure no one.

This first pool lasted till May, 1882; then, some members refusing to pay their assessments, it broke up. The distillers had been able to keep prices somewhat higher by its means; but after the breaking of the pool, they ran at low profits, many of them at a loss, or else shut down during the summer — a proceeding which in itself involved of course a decided loss. In September, 1882, they organized again for one year on a similar plan; but it was found necessary to make an attempt to limit the output of the distilleries to a small percentage of their capacity, in addition to the relief of the market by exporting.

It soon became evident that it was cheaper to limit production by paying some distilleries to suspend production entirely, permitting the others to work at more nearly their full capacity, than to limit all to a fixed percentage of their normal production.

Though the Kentucky product is of a different kind from that manufactured by members of the pool, it of course came into competition with the latter when it had aged enough to be put upon the market. The law allowing distillers to keep their product in bond for three years before paying the tax had led to a heavy overstocking in Kentucky, and when this stored product first began to come upon the market, the situation became still more trying.

From 1883 till 1887 the pool continued for a year at a time, with a suspension as often as once each year. Sometimes the better plan seemed to be to limit the output of the distilleries, leaving each distiller to attend to the marketing of the product himself; sometimes for the officers of the pool themselves to provide for the export of any surplus, assessing the individual distillers the amount required to pay any loss on the export. In the articles of organization of the pool of 1884, we read:

Only 28 per cent of the full capacity shall be operated, and no stocking up beyond this amount allowed under any circumstances. Any member operating his house and producing any kind of distilled spirits

must take care of them himself. The association is debarred from paying any member for maintaining any market, exporting goods, or warehouseing them.

In spite of the small percentage of capacity run during this year, the pool suspended in the spring of 1885, though it reorganized again in October of the same year. At the organization of this pool (in 1885) a committee reported:

It is the sense of this committee that no distillery shall be allowed to run beyond 40 per cent. The basis for market price should be fixed at the lowest possible figure, it being recognized by all that high prices are detrimental and difficult to maintain.

Section 12 of their articles of agreement, differing from those of the preceding year, provides for exportation as follows:

To maintain prices at all times, the officers shall cause to be exported at any time without the United States any surplus that may at any time appear, allowing and paying therefor [such] a bonus as will equal the quotation prices, and [shall] report all such exports, the quantity shipped, the bonus paid, etc.

Section 13 further provided that the president should cause a suspension of the association for the following causes:

If a distiller runs more than he is entitled to run; if a distiller refuses to exhibit his government book to an authorized agent; if a distiller refuses or neglects to make his monthly report or refuses to accept his draft or pay his monthly assessments; if a distiller resumes his capacity and operates his distillery having once sold it; in case exported goods are re-imported and placed upon the domestic market; in case closed houses are not paid in full, and in one payment, for each month, before the close of said month.

A resolution was also passed providing that the association be suspended when any new distillery should be built and start to run. Provisions were also made for the examination of the government books of each distiller by the officers of the pool, in order to prevent deception and cutting of rates on the part of any distiller; but in spite of these precautions, and in spite of the high prices they were able to maintain for their goods in the pool, it was found that the temptations to secure sales by

the cutting of prices were so great that members would violate the terms of the agreement. Within two months after its formation, in calling a meeting of the distillers whose houses were running, in order to determine the amount of assessments, prices of goods, etc., the president of the pool expresses clearly the state of the trade. It should be remembered, in considering his words, that they were written not to influence legislation or public opinion, but that they were addressed to men directly concerned, who knew the circumstances. Among other things, he says with reference to over-production and the proper policy of the pool:

That we shall over-produce after the holidays we all know — we knew it when we organized in Chicago and for that very reason made the assessment 12 cents on 40 per cent to create an export fund.[1] That we have already over-produced, figures will show. . . . A few more days running without a pool would have wound you up, and this over-production we are not trying to get rid of by exportation. You want to look these figures square in the face; and if it takes more money to do our exporting than you thought, it is occasioned by your own folly in over-producing so heavily in September and October. As long as we have funds to export the surplus there will be no difficulty in maintaining prices. When goods accumulate without any outlet, then is the time when cutting commences. . . . It will not do to make the price of goods too high, for as we raise the price we must raise the bonus on exports correspondingly. . . . There are but two things left for us to do; either provide sufficient means to keep our warehouses clear of the surplus by exportation, or let the market go to pieces of its own weight. I am well convinced there is cutting going on secretly now, and unless provision is made at once to arrest it, it will be done openly, until there is nothing left of the market. Situated as we are, the question is no longer as to making a great amount of money, but to prevent our suffering great losses. This is the problem for you to solve, and the meeting is called thus early as an imperative necessity, and all running houses should be present. Distillers, when they have an accumulation of goods on hand, will not hesitate to cut prices *one cent* a gallon to make a sale, when they will hesitate to pay one-half cent a gallon to make cutting *unnecessary*, even if double the amount is placed in their hands. Right

[1] That is to say, 12 cents for each bushel of capacity run, when the houses were running at 40 per cent of their full capacity. The capacity of a distillery is measured by the number of bushels of grain consumed per day.

here I will repeat what I have so often stated before, that the amount of the assessment does not come out of the distiller, but out of the consumer, the same as the government tax, and he [the distiller] is merely the agent to collect and pay it over, of course with the qualification that prices are maintained.

He closes a series of statistics (regarding the output in competing states) with the words:

I have been particular in giving you all the information possible, so you can act intelligently at the next meeting. The only way to maintain prices is to get rid of the surplus by exportation. You can fly in the face of Providence if you see fit, but it will bring its own punishment with it.

TABLE II

POOL ASSESSMENTS, SEPTEMBER, 1884, TO APRIL, 1887, INCLUSIVE

	1884 Cents per bushel mashed	1885 Cents per bushel mashed	1886 Cents per bushel mashed	1887 Cents per gallon
January		8	16	3
February		8	9	3
March		8	10	4
April		8	10 (Extra assessment for 1 day: 35 cents.)	4
May		7	10	
June		9	8	
July		9	4	
August		9	6	
September[1]	6		per bush. 2; per gal. 2	
October	6		per gal. 3	
November	8	12	" 3	
December	8	12 (Also extra assessment for 1 day: $1.50 per bushel.)	" 3	

[1] Assessment for September, 1886, was 2 cents per gallon produced (equal to 9 cents per bushel), and also an assessment of 2 cents per bushel; making a total of 11 cents per bushel. By multiplying the assessment per gallon by 4½, the amount per bushel will be obtained nearly. About 4½ gallons of spirits are made per bushel corn.

A pool seemed a necessity; but the experience of this and of the following year seemed to show that a pool could not be maintained. The competition, there can be no doubt, was for many ruinous, though those best situated could live and make profits. The difficulty in maintaining the pool, together with the effect of the pool on prices, may be seen in the fluctuating figures of Table III (page 37). The same movements are illustrated graphically in the Diagram (pages 42, 43), and there the changes may be more readily noted. Table II shows the extent of the assessments from September, 1884, to the time of the formation of the trust. It has not been possible to obtain the earlier assessments.

In consequence of the competition, and in order that a closer organization might be established, it was determined by the leading distillers, in the spring of 1887, to organize a trust, formed upon the model of the Standard Oil Trust. The "trust agreement," published in the examination of the president of the trust before the congressional committee in 1888, provides that the trust created shall be vested in nine trustees; that these trustees, under bonds of $100,000 each, shall, in accordance with section 11:

> . . . exercise supervision, so far as their ownership of stocks enables them to do, over the several corporations or associations whose stock is held by said trustees. As stockholders of said corporations they shall elect or endeavor to elect honest and competent men as directors and officers thereof, who shall be paid a reasonable compensation for their services. They may elect themselves as such directors and officers, and shall endeavor to secure such judicious and efficient management of such corporations as shall be most conducive to the interests of the holders of trust certificates.

No distillery was to be allowed to join this trust except the members of the former pool; but any member of the former pool, if a corporation, might join upon the assignment of a majority of stock by the individual stockholders to these trustees. For the stock thus assigned, the trustees prepared stock certificates, which showed the interests of each beneficiary in said trust. The certificates were divided into shares of the par

value of $100 each, and were known as the "Distillers' and Cattle-feeders' Trust certificates." Any distillery not owned by a corporation might be re-organized in corporate form in order, by the aforesaid assignment of stock, to join the trust. In accordance with section 4 of the trust agreement, no certificates could be issued except for stock, and the par value of the certificates issued were to represent as nearly as possible the actual cash value of the stock held by the trustees in trust. In estimating the value of the plants owned by the different corporations, the following elements were considered: (1) the cost of the construction of the plant; (2) the amount of working capital required for its management, and (3) its earning power. This last element, of course, depends upon various factors, and of necessity was left largely to the judgment of the committee appointed. The location of the distillery, the skill of its former managers, their ability to secure a sale for their product, and other factors would all need to be considered. Furthermore, the earning capacity of the distillery under the management of the trustees, if it should be allowed to run, might vary quite materially from its former earning power. These different considerations led the committee to issue certificates for from two to three times the cash value of the plants. This has led some of the critics to state that the trust certificates were about two-thirds water. A careful consideration of the factors involved will enable the reader to judge how far this is true.[1] That jealousy among the different corporations might be avoided, the value placed upon the stock of each corporation was not made known except to the corporation immediately interested and to the trustees.

The trust was to continue for twenty-five years from the date of its organization, and thereafter until terminated by a vote of sixty-six and two-thirds per cent in value of the holders of certificates, at a meeting called for that purpose.

At the first annual election three trustees were to be elected to hold their office for one year; three to hold their office for two years, and three for three years. Thereafter three trustees were to be elected annually to take the place of those retiring, each to hold his office for three years, except in case of those

[1] See Testimony of J. B. Greenhut before Committee of Manufactures, pp. 73 *et seq.*

elected to fill a vacancy, who should hold until the expiration of the term. A person to hold the office of trustee must be the actual owner of at least 500 shares of trust certificates.

The meetings of the certificate holders take place annually, and may be called oftener at the request of thirty-three and one-third per cent of value of the trust certificates.

It is to be noted that this trust agreement expressly provides that the trustees are not limited in their duties, as has been often suggested, to the receipt of dividends or interests upon the stocks or moneys held in trust, and to the division of such dividends to the holders of trust certificates; but they are also to elect competent men as directors and officers of said corporations represented, and are to exercise supervision over the several corporations whose stock is held by them as trustees. Furthermore, it is to be noted that these trustees in every case hold a majority of the stock in each corporation, so that their control over each distillery is absolute. A manager is appointed by the trustees for each distillery, whose salary is paid out of the trust funds. This manager is, of course, usually one of the leading original stockholders and managers in that distillery.

In order that the business may be kept well in hand, reports are required daily from each distillery engaged in manufacture; and each distillery that is running sends in a detailed report every month, showing the exact cost of manufacture of the product and all other details regarding the management of the business. Again, by these monthly reports the trustees are able, if they wish to lessen or to increase the amount produced, to close the distilleries that are working least successfully or to open those that furnish the best opportunity to supply any special market. The trustees are also at liberty to purchase distilleries that are running outside of the trust, and to lease distilleries managed by the trust, whenever in their opinion this plan seems more profitable than to operate them by trust officers. In the latter case, of course, the profits are still held under the control of the trust.

This firm control over the different distilleries enables the trustees to control the market by limiting the output of the product to the amount demanded rather than by exporting

the surplus at a loss, as was done under the old pools. Almost no attempt has been made by the trust to gain control of the foreign market, and none of the product has been exported at a loss since the formation of the trust. Their comparatively small exports (see Table I, page 25) have been at paying prices. A brief examination of Table II (page 30), which gives the monthly assessments levied upon the members of the old pool (from 6 cents to 18 cents per bushel) from September, 1884, to the formation of the trust in May, 1887, will show how great a saving has thus been effected.

Another saving is that which comes from the lessened expenses of management, resulting from the closing of so many distilleries. Nearly all the distilleries in the former pool, to the number of more than eighty, have become members of the trust. In order to limit the output to the demands of the market, these distilleries, if running when they joined, have been from time to time closed, until at the present time twelve distilleries supply the total amount that is placed by the trust upon the market. One or two others are running, but for the production of yeast, or some other product than spirits. It is by no means to be assumed that the decrease in the output corresponds in any manner with the number of distilleries closed. When it is taken into consideration that for several years the output of the distilleries had been often limited to from 25 to 50 per cent of their capacity, many of them even closing for portions of the year, it will be seen that an equal output might be produced by a much less number of distilleries. That there has been a smaller aggregate output is doubtless true, and that to an extent more than enough to balance the lessened amount exported. The amount is held in hand well enough, so that the trust can manage to control the market.

An examination of Table III (page 37), which gives the market prices of corn and whiskey from the time of the formation of the first pool, in 1881, to March, 1889, will show that the price of alcohol has not been to any noticeable extent raised by this closing of the distilleries. For some six or eight months after the formation of the trust the prices were lowered eight or nine cents per gallon, although the prices of corn ruled somewhat higher

than before. Presumably the purpose of this lowering of the prices at first was to bring pressure to bear upon the distilleries yet remaining outside of the trust in order to force them to join the trust, or else because in the beginning the trust did not yet have strength to force the market. After all or nearly all of the members of the former pool had joined the trust, so that its membership was practically complete, and it became evident that a contest with the distillers yet remaining outside was at hand, the managers of the trust raised the price. The new members would need dividends to keep them contented, and there was also a necessity of accumulating a fund upon which to enter upon this contest with their rivals.

A comparison of the prices of corn and alcohol for the year preceding the formation of the trust with the prices from May, 1888, to January, 1889 (see Table III, or Diagram), will show that the profits made by the trust have not been greater than those made by the old pool, unless the cost of management of the distilleries has been much decreased; and yet, during this period from May, 1888, to January, 1889, the trust had put the price high enough to enable them to pay good dividends to members that might otherwise have become dissatisfied and to accumulate a surplus for the purpose of a contest with outsiders. It is from this very evident that the saving in cost of management and manufacture has been very great. It must also be kept in mind that from twelve to twenty distilleries have been earning these dividends on stock that represents some eighty-three distilleries. This emphasizes still more the great saving effected in expenses.

The immediate result of this increase in price (from $1.05 to $1.09 per gallon, and then to $1.14) was the building of new distilleries, notably the large distillery at St. Paul; the opening of many small distilleries, and the manufacture of spirits by the smaller distilleries in Kentucky, whose normal product was whiskey for aging. When at length it became evident that the distilleries outside of the trust were also making a large product and the output from these distilleries was beginning to have its effect upon the market, the trustees, on the 1st day of January, 1889, again cut the price of the product to $1.04 per gallon, in

order to crush their opponents. The smaller distilleries in Kentucky and elsewhere of course closed promptly, or changed the character of their product. The most formidable rivals of the trust, Shufeldt & Co. of Chicago, who had doubtless also made large gains from the increase in price and who had run their distillery at even more than its normal capacity, at once cut down their output, though they have not closed and are even building a new house of 3000 bushels capacity.

What the next move will be, remains to be seen. It is said by the managers of the trust that their best policy is to hold the price of the product below the cost of manufacture by most of the rival distilleries and thus keep the market steady. They claim that they are able to do this from the saving in management and from the fact that they run only the distilleries most favorably located. For local trade they can run those that will save freight; and, in fact, they run one in Cincinnati, one in St. Louis, one in Kansas City, etc. The figures of the trust, gathered from the various distilleries under their control, show that the distilleries at Peoria have an advantage of from 14 to 15 per cent over most of the distilleries located elsewhere, so that here some six are running. It is the belief of distillers not members of the trust, as well as of the trustees, that a Peoria distillery has at least 10 per cent advantage over a distillery located at Chicago, and nearly 20 per cent over one located at St. Paul. This claim seems to be substantiated by the statement of Charles Clark, for many years past a prominent distiller at Peoria, though not now in the business himself. He says that at times of great depression in the business, during the existence of the former pools and earlier, his distillery made regularly 10 per cent on the running capital and 25 per cent on the plant, besides good salaries for the managing members of the firm. With the exception of one year this rate of profit was made for many years prior to the formation of the trust, and in that unfortunate year there was a clear profit of $12,000. During this very time the complaints of distillers in other parts of the country that money was being lost and that no interest could be made on their investments were doubtless often true. On the other hand, in estimating the ability of the trust to com-

TABLE III

MARKET PRICES AT PEORIA FOR WHISKEY AND CORN FROM 1881 TO 1888 INCLUSIVE

Month	1881		1882		1883		1884	
	Whiskey	Corn	Whiskey	Corn	Whiskey	Corn	Whiskey	Corn
January			1.15–1.16	62–59	1.13–1.14	44½–50½	1.15–1.16	41½–47
February			1.16–1.17	58½–54	1.14–1.15	48–55½	1.16–1.17	47–42
March			1.16	58¾–66½	1.15	56¼–49	1.17	41½–48
April			1.17	66¾–75½	1.15	47½–52½	1.17–1.12	43½–50½
May			1.13–1.17	75–70½	1.15	50–53	1.12	48–54½
June			1.11–1.15	72–69¼	1.15	53–47½	1.08	50–45½
July			1.11–1.14	73–75½	1.15	48–45	1.08–1.07	44–49
August			1.14–1.16	74½–77	1.15	45–51	1.05	47½–50½
September			1.16–1.18	75–59½	1.15	49½–46	1.10–1.11	51–45
October			1.16–1.18	61–70¼	1.15	45–47¾	1.11	40–53
November	1.11–1.15	62½–58	1.14–1.15	70½–67	1.15	46½–49	1.11–1.12	42–30
December	1.15	58½–62	1.13–1.15	55½–45	1.15	52–45	1.12	30½–35

Month	1885		1886		1887		1888		1888	
	Whiskey	Corn	Whiskey	Corn	Whiskey	Corn	Whiskey	Corn	Whiskey	Corn
January	1.12–1.14	34½–40	1.10	33–35	1.14	33¾–35½	1.09	48¼–47	1.04	30
February	1.14	38½–36½	1.10	34–32¾	1.14	35¼–33¾	1.09	47–45¼	1.04	29½
March	1.14	37¼–40½	1.10	33–34¼	1.14	33¾–38	1.09	45¾–49	1.04	30
April	1.14	39¾–47½	1.10	33¾–32½	1.14	37¼–36	1.09	47¼–53¼		
May	1.14	50–45	1.10	33–29½	1.14–1.05	37–38½	1.09–1.13	52½–57½		
June	1.14	44–47½	1.10	29–31	1.05–1.09	38¾–36	1.13–1.14	53¼–46½		
July	1.14	47–43¾	1.10–1.07	28¼–41½	1.05	38¼–34¼	1.14	49–43½		
August	1.14	45¼–42½	1.09–1.11	40½–39	1.05	38¾–42¼	1.14	45¾–40		
September	1.05	43½–40½	1.11–1.13	38¾–36	1.05	41½–39¼	1.14	44–40½		
October	1.04–1.09	42½–38½	1.13–1.14	35½–32½	1.05	39½–41¾	1.14	39¼–44		
November	1.09	44½–32	1.14	33¾–36½	1.05	39½–46	1.14	42½–38		
December	1.09–1.10	33½–31½	1.14	35½–33½	1.05	44¾–49½	1.14	33½–29½		

AVERAGE YIELD PER BUSHEL[1]

Year	Yield	Year	Yield	Year	Yield	Year	Yield
1881	3.694	1883	3.874	1885	4.076	1887	4.62
1882	3.792	1884	3.895	1886	4.55	1888	4.53½

[1] The average yield for the last three years is for the Trust or Peoria distilleries. The government report, including all distilleries, gives for the years 1886, '87, '88, respectively, the yield 4.09+, 4.23+, 4.24+.

pete with its rivals, it must be remembered that fourteen distilleries must make profit enough to pay dividends on the capital invested in more than eighty distilleries, a drawback amply sufficient to offset any slight benefit in the cost of manufacture. A distiller who has no closed houses to carry, no dividends to pay on capital that is inactive, has certainly something of an advantage. If the trust holds its own firmly, however, this advantage will soon to a great extent disappear, as the trust will doubtless, as opportunity offers, dispose of the useless closed distilleries and turn the dead capital into profitable channels.

The trust has, doubtless, had some benefit from the fact that dealers would fear to incur the hostility of so powerful an organization by purchasing from its rivals. This is again offset in part, by the popularity of certain brands of whiskey (though this would apply especially to the Kentucky product) the manufacturer of which can always be sure of his market. It is probable, at any rate, that the advantage is not so decidedly with the trust that it can totally crush out all competition, though this can be determined more certainly after a year or two. At present it manufactures only from 80 to 85 per cent of the total product in the market, and its rivals are preparing to compete still more vigorously. Shufeldt & Co. of Chicago, as has been said, are building a new distillery, and there are reports that others in Illinois are soon to be built. The trust cannot afford to buy out all distilleries that may be built. If it is to succeed, it must keep its prices so low that new distilleries will not be built. Its action in pushing up the price last year, if a merely temporary expedient to accumulate a fund, was perhaps a wise move from the standpoint of the trust; but such prices, quoted too often, would not be of advantage. The trust must succeed by underselling its rivals, not by buying them out. This is evidently, too, the policy of the organization; for it is a rule that no distilling company not in the old pool can join the trust. Even those companies have not been coaxed in by too large offers, as is sometimes asserted. The assertion made in the New York *Evening Post* of January 2, 1889, by the agent of Shufeldt & Co., that the trust had tried in many ways to force that firm into union, and had even offered it $1,000,000 in

cash to join the organization is, even if correctly reported, not true. Both the trust officers and Shufeldt & Co. deny it. Doubtless the trust would be glad to be joined by so important a rival; and it is conceded by members of the trust that, had the company joined them when the trust was organized, its managers could have had much influence in the new organization. The implication is that they might have had a trustee. It is worth while to give this much of the case, because it shows the position the trust has taken regarding perhaps its most formidable rival, and the course it must pursue if it is to succeed. It must meet its competitors in fair business rivalry and be able to control by low prices the larger part of the sales.

As much is said regarding the influence of trusts and combinations of all kinds on wages and prices of materials, it may be worth while to mention the statements on this subject furnished by the president of the trust to the congressional committee. The coopers that manufacture barrels for the distilleries and the miners that furnish coal both testify that the distilleries connected with the trust voluntarily raised the prices for barrels and coal so that fair wages could be paid. Before the organization of the trust such a rise in prices could not be given on account of the fierce competition, and even after its formation distilleries not connected with the trust held the miners to their former oppressively low contracts, instead of following the example of the trust. The president of the trust adds that while they "do not wish to take the position as posing before the public as benefactors to any extent," yet they do believe in "the principle of intelligent coöperation," and as they can afford to pay good wages they are willing in justice and fairness so to do.

Most of the advocates of trusts and pools claim that one of the chief advantages to come from them is *stability* of prices. An examination of Table III, or better, of the Diagram, will show that while the fluctuations are somewhat less frequent under such a régime, yet, when a fall or rise in price does come, it is sudden, and is apt to be a change of considerable extent. It is very questionable if there is any gain from such a policy. The lack of stability under the old pool was due, it was claimed,

to the instability of the pool itself; but so far matters have been little better in this respect under the trust. One thing seems better under the trust: the trust itself has stability, and seems to have power; it may steady prices if it will put them somewhat low and be satisfied with moderate steady returns, instead of striving for great gains interspersed with very small ones. The future will determine what is to be its policy. The managers of the trust say that the policy of the trust is to secure steady, moderate gains; others who are interested question this. The system of high gains alternating with low ones, if pursued as a regular policy, would do much to justify the distrust of the public and would take away the only ground on which such combinations can fairly be justified: low, steady prices.

A sufficiently accurate estimate of the real benefits accruing to the various distilleries from their association in the trust may be obtained from an examination of the dividends paid by the trust since its formation, and from the value of the trust certificates. Although the trust was organized in June, 1887, many of the distillers belonging to the old pool had not been received into the trust until about the beginning of the following year; so that any dividends paid before January, 1888, cannot be considered fair tests of the management or of the success of the trust. From January, 1888, to July, 1888, inclusive, a dividend of one-half of one per cent per month was paid; for August the dividend decreased to one-fourth of one per cent; and from September till January, 1889, inclusive, dividends of one-third of one per cent per month were declared. The dividend for February, 1889, again decreased to one-fourth of one per cent, owing doubtless to the late cut in price. It must be borne in mind, also, that in addition to the dividends throughout the year 1888, a surplus was being accumulated to carry on the contest with outside distillers. It was said by some members of the trust, when the trust certificates were valued at 30, that they then represented about the actual cash value of the plant. If this be accepted as an accurate estimate, and it is doubtless not far from the truth, we can readily see that the trust has paid dividends, during somewhat more than one year of active existence, of more than 12 per cent per annum.

TABLE IV

QUOTATIONS OF MARKET VALUE OF DISTILLERS' AND CATTLE-FEEDERS' TRUST CERTIFICATES

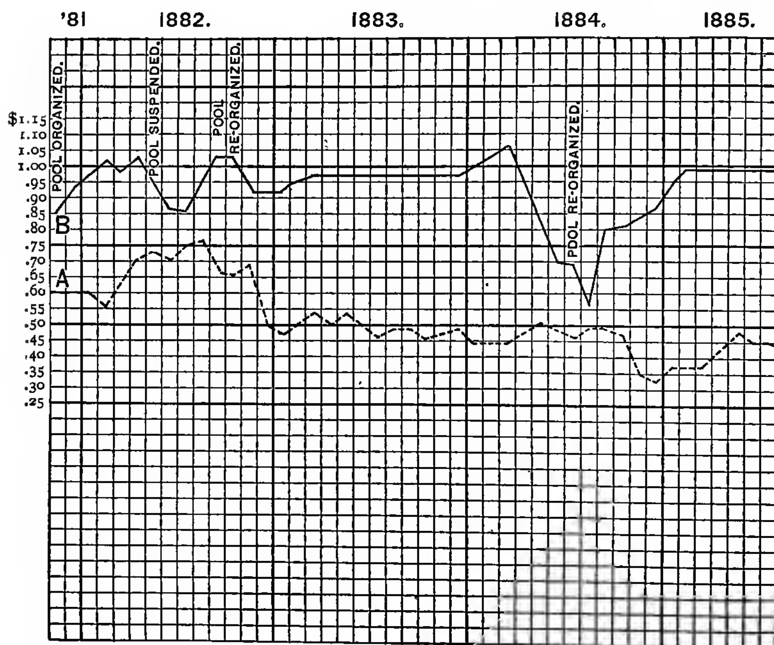
1888.	March	1.	50.	1888.	Aug.	28.	43.	1889.	Jan.	15.	30.
		14.	48.		Sept.	7.	40.			31.	31.
	April	1.	45½.			19.	39½.		Feb.	9.	32.
		20.	42½.		Oct.	10.	36½.			18.	33.
	May	11.	45½.			20.	35½.		March	4.	34.
	June	4.	43.		Nov.	13.	39.			7.	35.
		18.	40.			21.	39.			13.	36½.
	July	2.	41.		Dec.	12.	35.			20.	35½.
		7.	44.			21.	33.		April	1.	34.
		24.	45.	1889.	Jan.	4.	33.			6.	34.
	Aug.	13.	42.								

An examination of Table IV, which gives the value of trust certificates for each month from March, 1888, to the present time, will lead us to about the same conclusion. As soon as it became evident that the trust was firmly established and bade fair to be a success, some small sales of certificates were made to enthusiastic buyers as high as 65; others among distillers at 55; but no real market for trust certificates was established above 50. With some slight variations the value has slowly decreased, until in January, 1889, the lowest value (30) was reached, since which time a slight increase in value is to be noted. The figures in this table are based upon actual sales, and there can be no doubt as to their accuracy. It is, however, to be remarked that the certificates are held mainly by the large distillers as investments (though the number of individual certificate holders has largely increased), and that comparatively few transfers of trust certificates have been made. The prices quoted of course depend, too, to some extent, upon the amount invested at the time. The certificates are not listed in any stock exchange, and there cannot be said to be any regular market for them, though they can be obtained through brokers in four of the principal cities: Peoria, Chicago, Cincinnati and New York. The figures given represent, then, almost with perfect accuracy, the value placed by the distillers and the liquor dealers upon the certificates.

The facts given with reference to the working of the trust

seem to show that it has been beneficial to the greater portion of the manufacturers of alcohol and spirits in the United States, although individual distillers have perhaps made no more, and some, it may be, have made even less profit than they could have made acting independently; while, so far at least, the prices to consumers have not been on the whole increased, and the tendency seems to be towards lower and steadier prices for the future. As has been said, however, only the future can

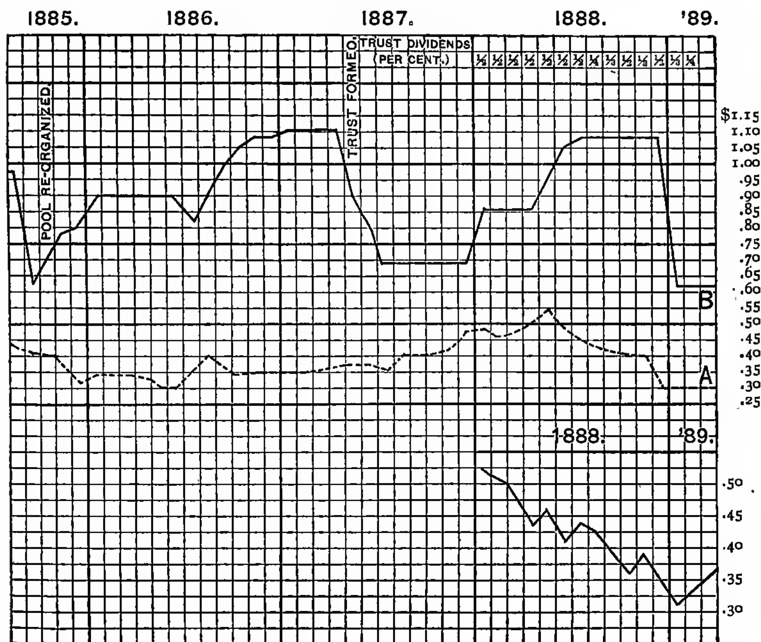
DIAGRAM ILLUSTRATING THE HISTORY



The (dotted) line A shows the average market value of corn per bushel at Peoria. The line B shows the average market value of the whiskey (the spirits used for base in prices) from one bushel of corn. To obtain this value, the revenue tax was deducted from the market value of one gallon, and the difference multiplied by the average yield per bushel of corn. — The space between the lines A and B represents, of course, the cost of production plus the profits. During the greater part of the pool's existence, assessments for export expenses must be deducted from the profits. (See Table II.)

determine what the policy of the trust is to be. The facts seem to show that it is within the power of the trust to bring about this result; and it seems to be for its interest so to do. As regards the stronger rivals of the trust, the prices have so far been so high that they have not suffered materially. The next year or two will show whether they can endure the competition. Even if they should be forced to close, the question is still an open one whether more distilleries would have not been closed

OF THE WHISKEY POOLS AND TRUST.[1]



The line in the lower right-hand corner shows the fluctuations in the value of the trust certificates: par value, 100; cash value of plant estimated at about 30.

[1] Professor Jenks, in his *Trust Problem*, N.Y., 1902, p. 146, continues this price diagram to 1900. Much other information is in the Reports United States Industrial Commission, Vol. I, 1900. — ED.

under free competition. Many stockholders are now drawing dividends from the trust who, without the trust, would doubtless have lost much of their capital.

At the time of the formation of the trust, it was thought by some of the distillers living at Peoria that, on account of their unusual facilities for manufacture, the trust should be limited to Peoria distilleries and a few others favorably located. The experience of the trust seems to show that, had this plan been followed, the trust might have paid higher dividends to its members and might also have held the price of alcohol so low that outside competition would not have been much more successful than it has been under the present arrangement. Some distillers who believed in this latter plan — presumably for the most part Peoria manufacturers — still think it would have been better to have limited the organization to five years with the option then to continue, suspend, or reorganize. They feel that the owners of the less favorably situated distilleries have an undue advantage. Of course, this depends mainly upon the relative value placed upon the plants when they entered; but it is probable that it would have been cheaper to crush some of the weaker members than to buy them by admitting them to draw dividends. Against this view is, of course, the fact that such action would have aroused bitter hostility that might well have resulted in the building of new distilleries in locations where they would have become formidable rivals.

On the whole, while there is this slight tendency to think that matters might have been better under some other form of organization, or even, for a few, with no organization; and while there may be a slight feeling that the trustees are not entirely free from nepotism in their appointments, any more than are our highly esteemed executive officers of the United States; yet, as was shown a year ago by the unanimous reëlection of all the trustees at a meeting in which ninety-nine and one-half per cent of all the certified holders were represented, as well as by the general expression of satisfaction on the part of the distillers one meets, the trustees are thought to have performed their responsible duties with descretion, and the trust is considered by its members a success.

J. W. Jenks

The later history of this combination has been checkered. In 1890, it was reorganized as a corporation, as the Distilling and Cattle Feeding Co. Its ownership of distilleries was extended to practically all important competitors. In 1893, failure impending because of the accumulation of floating debts for unpaid rebates, bonds were issued. For two years various scandals, mainly speculative, developed under its control by receivers; and the Supreme Court of Illinois in 1896 ousted it from its franchises (156 Ill. 448). Meanwhile in 1895 it had been again reorganized as the American Spirits Manufacturing Co., incorporated in New York. This company took over all the best distilleries in the field. Other plants and branches of the business were independently incorporated under the laws of New Jersey during the next four years in three principal companies. These were again united to the main stem in 1899, as The Distilling Co. of America, capitalized at $125,000,000. Over ninety per cent of the securities of this company in 1902 were in turn acquired by a holding or finance company, the Distillers' Security Corporation of New Jersey, which has issued about $50,000,000 of capital stock. — Ed.

Note. W. S. Stevens, Industrial Combinations and Trusts, 1913, pp. 4 and 36, reprints texts of agreements. His chapters II and IV give additional data on the legal trust form of organization. Standard Oil experience is outlined in Chapter XVII, *infra.*

III

THE WIRE-NAIL ASSOCIATION OF 1895-96 AND OTHER IRON AND STEEL POOLS[1]

SO lately as 1888 *The American Architect* began an article on nails in this way: "The nails commonly used in connection with building operations are too well known to require any description. They are specifically designated as plate nails." That year, 1888, was almost the first in which plate or cut nails felt a real competition from wire nails. In that year the latter formed less than a fifth of the total product; in 1895 they constituted nearly three fourths. The idea of making nails of wire did not arise in America; in fact, our people were even somewhat slow to adopt it. The first wire nails — headed by hand and ground to a point — appear to have been made in France early in this century. Mr. M. Baackes, an old wire-nail manufacturer of Cleveland, says that the first machine for forming the heads was made in France about 1850. According to Mr. John Hassall, who is still engaged in making wire-nail machinery in New York city, his father was active in making and running the first wire-nail machines used in this country, early in the fifties. The business seems to have extended itself only modestly, for Mr. Baackes regards the factory which he helped to start at Covington, Ky., in 1875, as "the first mill for the manufacture of wire nails on this side of the Atlantic." The production rose from 20,000 kegs in 1880, according to Mr. Baackes's estimate, to 125,000 in 1887; and the average price fell from $20.00 per keg in 1875 and

[1] From the *Political Science Quarterly*, Vol. XII, 1897, pp. 246-272. Some footnotes are omitted on account of lack of space. For the best analysis of modern pools, one should consult W. S. Stevens, *American Economic Review*, 1913, pp. 545-575. — ED.

$10.00 in 1880 to $4.81 in 1887. At the end of 1887 a manufacturer wrote: "Wire nails are now quoted at less than actual cost, as results will in time demonstrate."[1] About the same time the *Iron Age*, the leading paper of the hardware trade, said editorially: "It is evident that the business is now greatly overdone."[2] The production increased, however, to more than 300,000 kegs in 1890, and to nearly 600,000 kegs in 1895; and the average price fell to $2.85 in 1890, according to the estimate of Mr. Baackes, and to $1.60 in 1894. At present, April 1, 1897, it is about $1.50. These facts show how recently and how rapidly the business has attained importance, and how fast the price of wire nails has fallen.

The profits of the early wire-nail men, as first comers in the field, were doubtless good; but the cost of production at that time must not be gauged by the later selling prices. At the outset their machinery was imperfect. Then, the first nails were of small sizes, for special purposes, such as use in cigar boxes, furniture, mouldings, and wagons; and small nails are relatively costly. It was not till 1886 that a list of regular or "penny" nails was published, and a serious effort was made to compete with cut nails in the general market. The wire of the first makers, too, was all of Norway iron; for they could not get any other material on which they could form a head that would not break off in driving. The H. P. Nail Co., established in 1879, is said to have been the first to succeed in using Bessemer steel wire. Finally, the price of Bessemer steel itself was at first much higher than now. Although quotations on steel billets earlier than 1887 are not available, their fall in price may be gauged by that of steel rails, which dropped from an average of $48.25 per ton in 1879 and $67.50 in 1880 to $37.08 in 1887. Billets were $32.55 on the average in 1887 and $16.58 in 1894,[3] while they are now quoted at about $15.00. It was the removal of these early limitations that made possible the great expansion of the industry.

As the business is now carried on, regular nails are sold with reference to a "base price" and a uniform schedule, or "card,"

[1] *Iron Age*, Jan. 5, 1888, p. 22. [2] *Ibid.*

[3] Report of American Iron and Steel Association, 1896, p. 26.

of "extras." Excepting under the card made in 1895, the base has always been the same as the price of the largest nails. It is the base only that is named in market reports and in quotations. The extras, which are added to the base to determine the prices of the smaller sizes, are fixed by agreement of the manufacturers, and are likely to remain unchanged for several years together. From April 11, 1892, to July 19, 1895, the card was as follows:

60-d.	base (no extra)
50-d.	$.10 extra
30-d. and 40-d.	.25 "
20-d.	.35 "
12-d. " 16-d.	.45 "
10-d.	.50 "
8-d. " 9-d.	.60 "
6-d. " 7-d.	.75 "
4-d. " 5-d.	.90 "
3-d.	1.20 "
2-d.	1.60 "

When 60-d. nails were quoted at $.85, put up in a keg which I am assured by a manufacturer cost at least $.09, the wire from which they were made was quoted at $1.15. Every nail-maker who bought his wire in the market lost the whole cost of handling and manufacture, and nearly four-tenths of a cent besides, on every pound of 60-d. nails he sold. The explanation of his apparent willingness to sell below cost is found in the character of the list of extras, and in the manner in which all orders were required to be assorted. The extras on all the smaller nails were far greater than the differences in cost between them and the largest. Indeed, the wire for a keg of 12-d. nails cost no more than that for a keg of 60-d. No manufacturer would sell 60-d. alone at the market price. All orders had to be so assorted that the average of the extras on the whole should be at least $.60 per keg: that is, if a dealer gave an order for a hundred kegs, at a base price of $.85, he had to make it up in such a way that the average price of the whole, by the schedule, would be not less than $1.45. So the loss on the larger and cheaper sizes was covered by the gain on the smaller and dearer. Some small manufacturers took advantage of this artificial ad-

justment of prices, by making only the smaller sizes, and leaving the losing end of the schedule to the great establishments.

I. History of the Association

Iron and steel products have been particularly fruitful of combinations; but before 1895 circumstances had not been favorable to bringing wire nails into the list. The manufacturers had been fairly contented, making the comfortable profits of a new and rapidly growing business. It is probable that combinations are not easily formed in any industry so long as the average man of those concerned, with average advantages, can make such a profit as the general opinion of business men pronounces fair; and that consolidation generally results from a strong sense of pressure. In this business, by the beginning of 1895, the necessary pressure had developed. The manufacturers cried out with one voice that they were ruined by competition. It must be noted, however, that most men do not consider it good policy, under any circumstances, to magnify their profits before the world; that men who have been accustomed to large profits do really imagine themselves ruined when they are reduced to not much more than ordinary interest on their capital; and that lugubrious statements, made in general terms and without figures, ought not to be taken without salt. The bulk of the wire-nail business was in the hands of six or eight great companies, which had their own wire mills and rod mills, and put the material through all the processes from the form of the steel billet. So long as smaller concerns, buying their wire in the market, continued to do business, it strains credulity somewhat to believe that the great establishments did not make moderate profits. The curious arrangement of the schedule of extras does seem to have given a certain opportunity to small makers; but the matter was in the hands of the great companies, and they would have changed the schedule if they had found it to work strongly against them. The strict requirement of assorted orders made it impossible for any maker of small nails only to do more than a very restricted business. If any dealer bought many nails of such a maker, he could not buy his large nails at the market price.

The days of good profit to the average man with average advantages were, however, gone by; and the manufacturers — large and small alike — were in a state of mind to yield themselves plastic to the hand that could organize the machinery for increasing profits. This hand belonged to Mr. John H. Parks of Boston, who had been a member of the old firm of Loring & Parks, long well known as manufacturers of tacks. That firm combined with their principal competitors, some six years ago, in forming the Atlas Tack Corporation, which is still the giant of the tack trade; though the leading men connected with it have thought it well during the last few months to put it through a receivership and a reorganization, with the usual absorption of the interests of the smaller investors. For several years past, Mr. Parks has confined his personal attention to the promotion of combinations in various lines of hardware. Bolts and shovels, as well as tacks and nails, have known his supple hand. From a time early in the spring of 1895, he seems to have been busy in working up an agreement among the manufacturers of nails. The approaching consummation of this enterprise was announced on May 2, through the *Iron Age*, in the following words:

> With a view to securing a better condition of things and correcting influences which hitherto have tended toward irregularity in prices and the unsettling of the market, the manufacturers have been conferring with a view to concerted action in this direction.

The combination began its activity with the customary declaration as to its moderate purposes with respect to price. In the article from which I have quoted, this vital matter is thus dealt with: "The manufacturers directly concerned in the movement disclaim any intention of advancing prices unreasonably, their purpose being to market their goods at a reasonable profit."

The first effect of the rise of the combination was a press of orders. Many jobbers bought all the nails that they expected to need for six months or more. From about May 1 the manufacturers refused to accept any orders for shipment later than May 30. By May 15 the base price had risen to $.95; and by

the 20th it had become so difficult to place large orders that there was no quotable price. Some sales were, however, reported about this time at $1.15 to $1.20. The combination was formally completed in the last week of May, and the base price for June was fixed at $1.20, for car lots, f. o. b. Pittsburg. All nails, no matter from what mill, were to be sold, freight paid, on the basis of the Pittsburg price, plus the rate of freight from Pittsburg to the point of destination. For instance, a customer at Anderson, Ind., would have to pay a base price, consisting of $1.20 plus the rate of freight from Pittsburg to Anderson, whether he bought in Pittsburg, or in Cleveland, or from the mill in his own town. Jobbers were allowed a discount of five cents per keg on purchases of a thousand kegs from one mill within one calendar month; and the minimum was soon reduced to five hundred kegs. In addition, a rebate of ten cents per keg, payable after six months, was offered to jobbers who should neither buy any nails from outside makers nor sell below the association price.

The form of the association was that of a simple pool. Prices and output were always fixed for a month in advance. The agreed production was apportioned to the companies on a basis depending partly on sales for three months before the pool was formed, partly on production in one of those three months, and partly on capacity as indicated by the number of machines. Any mill could sell its privilege of production, or any part of it; but every mill was rigidly restricted to its allotment during each calendar month, unless it bought the allotment of another. A cost price was assumed, which was supposed to represent the cost of production at Pittsburg; and the cost at every other point was assumed to be equivalent to the Pittsburg cost with freight from Pittsburg added. This was because the raw material comes chiefly from the Pittsburg region. So the selling price, including delivery at the buyer's railroad station, and the assumed cost price were harmonized by the use of the Pittsburg base. All the profits, above the cost prices so arrived at, were paid into the pool; and the amount in the pool, after paying all expenses, was divided monthly. The basis of division was the same as the basis for the allotment of production.

An inspector, hired by the association, was placed at each association mill, with the most sweeping powers of investigation. Every part of the mill, every book, every letter written or received, was open to him. So far as possible, outside owners of nail machines were hired to keep them idle, and makers of machines were hired to refuse orders for them from persons outside the association. For a year it was very difficult to buy a machine, and while the association lasted it was never easy. A company which went into the business in the autumn of 1896 writes:

> We found the market in which we could buy machines was very limited, most of the machine manufacturers having entered into an arrangement with the combination to stop making them for outside parties. We were unable to obtain what we wanted, and consequently our production of nails was much below what we intended it to be when we started.

With a similar combination of Canadian nail manufacturers, the association made an agreement by which each bound itself not to offer goods in the territory of the other. Efforts were also made to induce the European manufacturers to agree to let none of their nails come to America. Although it is said that they did not meet with much success, only one large lot of nails and a few small lots were actually imported during the existence of the pool.

The agreement of the wire-nail men was accompanied by a similar agreement of the cut-nail men. Although separate in form, these two organizations acted as one. The price of cut nails was accordingly advanced with that of wire nails, at first 20 cents below, and afterwards uniformly 25 cents below — a difference not relatively greater than that which had existed before the pool was formed. Wire nails were so far preferred that, in spite of the difference in price, their competition had reduced the trade in cut nails to a fraction of its former size, and had thrown hundreds of cut-nail machines out of use. The existence of these machines was one of the chief sources of embarrassment to the two associations. The wire-nail pool had to turn over large sums to its weaker associate, to be used in

paying the owners of these old cut-nail machines to keep them idle.

The demand for nails continued very strong through June. The production for the month had been restricted somewhat, in order to insure control of the market. Before the 12th the mills had sold their entire allotments for the month and were refusing all orders.[1] Yet, at their meeting held the week following, they made a further restriction of their output for July, reducing it to about half the average monthly product for the previous year,[2] and fixing the price for July at $1.55. Dealers anticipated a further advance, and in their desire to protect themselves clamored for nails. Before July 4 some manufacturers had sold their entire allotment for the month and were again refusing orders. By the 10th, few nails could be bought from manufacturers.[3] On July 18 a new "card," or schedule of extras, was adopted. The extras on 10-d. and smaller nails were not changed; but all larger sizes were put on an equality with 10-d., with an extra of 50 cents. The requirement of assorted orders, or a minimum average of extras, was abolished; but the lowest extra was now almost up to the old required average. The base price for August was made $2.05.

The success of the nail combination had been followed by a sharp and general advance in the prices of iron and steel products, and had doubtless contributed to cause it. A market report of May 30 said: "Billets are $17.50 and will likely be higher, and the agreement reached by the wire-nail mills is also having its effect on rods, and prices are very much higher."[4] Between May 1 and August 1 plain wire, from which nails are made, rose from a base price of $1.10 per cwt. to $1.50; wire rods, from which wire is drawn, from $21.00 per gross ton to $29.00; steel billets, from which rods are rolled, from $15.50 per gross ton to $21.50. There seems to have been what is called a good understanding between the producers in these lines, but no formal combination. On August 22, however, this announcement appeared: "The barb-wire trade has been organized on the same lines as the wire-nail trade. A sharp

[1] *Iron Age*, June 13, 1895, p. 1248.
[2] *Ibid.*, July 11, 1895, p. 85.
[3] *Ibid.*
[4] *Ibid.*, May 30, 1895, p. 1143.

advance in prices has been made. Plain wire will likely advance in sympathy with barb wire."[1] On September 5 it was announced that prices of plain wire had been advanced, "as the result of an understanding arrived at by the manufacturers." The base price of wire nails was advanced to $2.25 on September 1, "in view of the increased cost of raw material." The demand had continued good during August. In the latter part of the month, in consequence of the restriction of output, there had been some scarcity. In September the demand began to fall off notably, but the mills disposed of their allotments for the month. Trade was poor in October, and in November it was very light. The manufacturers complained particularly of the large stocks which the jobbers had on hand, and which some of them were offering rather under the combination price. The pool was strengthened in November, however, by the accession of several companies which had been operating outside.

About November 25 the only large lot of nails which has been imported into this country in many years was received by the Bigelow & Dowse Co., of Boston. Rumor puts the amount at about 5000 kegs, or 20 carloads. Several small lots were received at New York during the next year, but the largest is not believed to have exceeded 500 kegs. It is not known by what means the Bigelow & Dowse Co. were convinced that it would be better not to repeat their operation; but apparently they did not cut the association price, and they brought in no more nails. Jobbers, who investigated the matter with a view to importing, say that English nails could not at any time have been imported with profit, but that German and Belgian nails could have been laid down in Boston or New York at from 50 to 70 cents below the highest price reached by the pool, even after paying the duty of 25 per cent. It required more courage than appears at first sight, however, to venture on placing foreign orders. The German and Belgian nails are shipped in bags, and to make them salable in the American market they must be kegged after receipt, at an expense of from 10 to 20 cents a keg. The head is formed a little differently from that of the American nail, and the tendency of human nature to

[1] *Iron Age*, Aug. 22, 1895, p. 404.

reject the unaccustomed might cause some objection to it. But the chief deterrent of imports, aside from the tariff, was the power of the pool to drop the price at any time to a point that would cause the importer a very serious loss. Nothing would have been so likely to cause a drop as the fact that large foreign orders were being placed.

The duty on nails does not now serve any purpose except to increase the power of combinations. Nails are produced here as cheaply as anywhere in the world, and are regularly exported. The duty does not protect the industry, and under full competition does not affect the price. But if there had been no duty when the pool was organized, either it would not have been organized, or it would have had to content itself with a much more moderate advance. An excessive advance would have caused the other obstacles to importation to be overcome, and would have led to free purchases abroad.

In December the manufacturers gave jobbers a guaranty on their December purchases against decline in January: that is, they agreed that, if they made a reduction of price in January, they would give jobbers a corresponding rebate on such nails bought in December as they had still on hand. This policy was thereafter followed from month to month till near the breaking up of the association. It was meant to induce freer buying by the jobbers; but its success was slight. The demand for nails was exceedingly light during the winter, and the stagnation propagated itself back to the market for raw material. In a market report of January 2, 1896, is this remark: "Until there is an improvement in the wire and wire-nail trades, it is not likely there will be any demand for rods." On January 16 it was stated from Pittsburg that no sales of rods had been reported in that market for some time. Early in February the nail association announced an advance of 15 cents, to take effect March 1. This galvanized the market into a mild, convulsive movement. The operation was repeated in April, with an announcement of an advance of 15 cents to take effect May 1. Trade was very dull, however, and the manufacturers admitted that the market was a good deal disturbed by outside nails and by the offerings of jobbers. High prices had so curtailed con-

sumption that a considerable quantity of nails, bought before the pool was formed or in its early days, was probably still in the jobbers' hands. These formed a disturbing element, in addition to the growing production of outside factories.

About April 1, 1896, the makers of steel billets formed a pool. The amount of billets in the hands of middlemen, or contracted for by them, was so great, however, that the attempt of the pool to raise prices $3 or more per ton was only partially successful. The wire-rod makers also tried to form a pool, but after much negotiation were unable to agree. Their good understanding, however, seems to have continued.

Early in June the nail association succeeded in coming to terms with the Pittsburg Wire Co. and Baackes & Co., of Pittsburg, by which these companies agreed to stop making wire nails. Their nail mills were by no means of the first rank; but they were large enough to make a considerable figure in the market under the existing circumstances of very small consumption, and they had been selling somewhat below the association price.

If the statements of the manufacturers could be accepted freely, we should need to explain to ourselves the rather curious phenomenon of producers keeping the price of their product abnormally high, contrary to their own desires, in deference to the wishes of their customers. It was semi-officially announced that while the manufacturers came to their meeting on June 3

> with the general expectation that some action would be taken looking toward a reduction in price, they were confronted with many letters from jobbers emphasizing the injury that would be done to the market by the reduction in the price of so staple a commodity as nails, and urging the manufacturers to maintain existing prices.[1]

Such a phenomenon would not have been inexplicable if it had existed; but an examination of twenty-nine letters of jobbers on the situation, published about that time, indicates that it was essentially a myth. Two of these regarded the price as a matter which concerned no one except the manufacturers, and which no one else ought to trouble himself about. Only seven could be counted against an instant reduction, on any construction of their words. Nineteen either were opposed

[1] *Iron Age*, June 11, 1896, p. 1384.

to the existing high prices or at least went so far as to say that, if a reduction were to come before January 1 (a matter on which they expressed no opinion), it had better come at once. The retailers were unanimous for reduction, complaining of a great falling off in their sales, which some put as high as fifty per cent. They reported that building and repairing were much interfered with.

Meantime a growing number of small mills gave the association increasing annoyance. By July 1 it was estimated that 25,000 kegs a month were made by outside mills. The total sales for June, by the association and outsiders, were estimated at 90,000 kegs;[1] while it was said that the allotment for July was 65,000 kegs,[2] and that the associated manufacturers did not sell so many.[3] These statements were made by the Pittsburg office of the *Iron Age*, which was at the centre of the movement, and which ought not, it would seem, to have sent out any but well-founded statements — at least about matters so definitely fixed as the monthly allotment. There is reason, however, for supposing that these figures were too low. A man who knows the innermost history of the combination has said that he does not think there was any month in which the manufacturers in the pool did not sell 150,000 kegs. This statement seems modest enough, considering that the average monthly production for 1895 was nearly 500,000 kegs.

Rumors of concessions and irregularities in price increased. On September 1 the guaranty to jobbers on each month's purchases against decline in the succeeding month was discontinued. It was noted with satisfaction that, in spite of the low prices which had to be made to meet foreign competition, the export trade was assuming relatively large proportions.[4] Early in September several outside manufacturers were induced, on expensive terms, to withdraw from the market. It was claimed that the production of those still outside was insignificant; but, in spite of this claim, the association lost its grip on prices to an extent far greater than at any earlier time. Chicago was the centre of greatest disturbance. Nails were openly offered there by jobbers

[1] *Iron Age*, July 23, 1896, p. 186.
[2] *Ibid.*, July 30, 1896, p. 236.
[3] *Ibid.*, Aug. 13, 1896, p. 334.
[4] *Ibid.*, Sept. 10, p. 512.

at $2.50, and finally at $2.25, for small lots from store, for which the association price was $2.80. The demand, however, showed a great improvement in September, and it continued good in October. It was estimated that the total output for October would be about 250,000 kegs,[1] or about half the average monthly output for 1895. Soon after October 1, the manufacturers succeeded in patching up the trouble at Chicago; and about the 15th the market reports said that there was "not a suspicion of weakness in any direction," and that the association had "demonstrated its ability to control the situation." It was, nevertheless, hardly two weeks before the final break appeared. About November 1 Chicago jobbers began to offer nails from store at $2.40. The break spread rapidly, and by the 10th the association price was merely nominal. Demand continued light. No one bought more nails than he had to have, because to-day's price was always likely to be bettered to-morrow. About November 20 nails were openly offered at Chicago at $1.50 by representatives of association mills. On December 1 the association held its last meeting, adopted a new card of extras, and formally dissolved. The new extras on common nails are as follows:

20-d. to 60-d.	base
10-d. " 16-d.	$.05
8-d. and 9-d.	.10
6-d. " 7-d.	.20
4-d. " 5-d.	.30
3-d.	.45
2-d.	.70

This schedule makes a large reduction in the relative price of small nails, which was undoubtedly intended to shut out the small manufacturers who had been making small nails only. The new card, however, comes much nearer than any previous one to representing the relative cost of large and small nails, under present conditions of manufacture.

II. The Course of Prices

When it is said that nails were selling on May 1, 1895, at $.85, and that on May 1, 1896, the association made the price

[1] *Iron Age*, Oct. 29, 1896, p. 837.

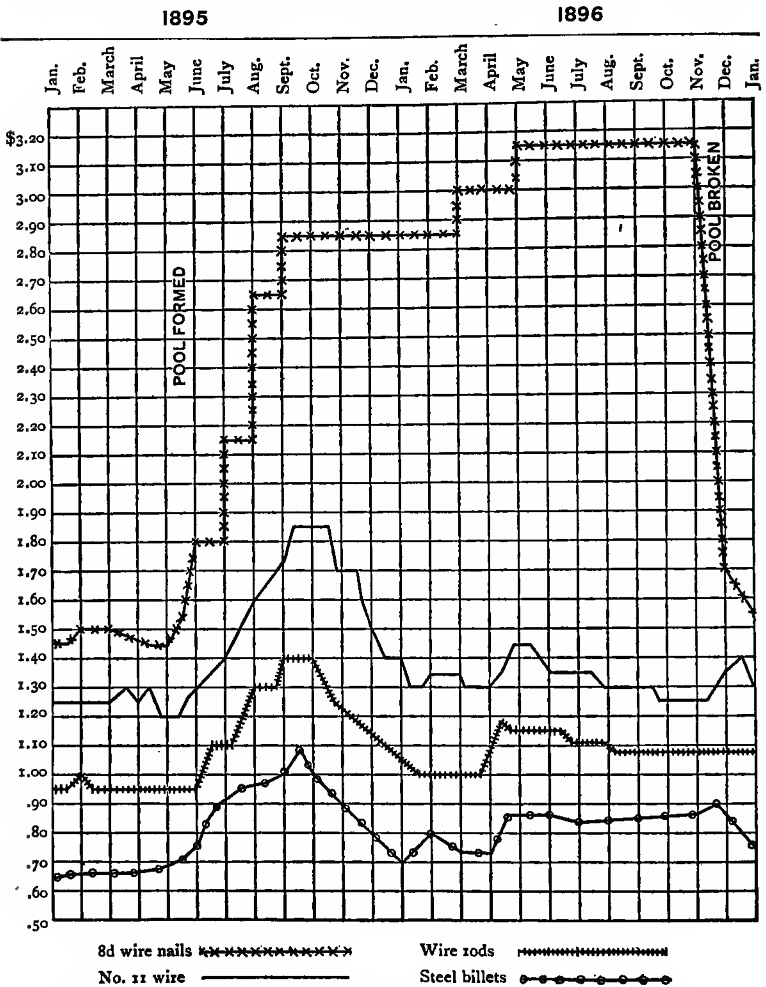
$2.55, the price appears to have been multiplied within a year exactly by three. The case looks still worse when it is said that 60-d. nails sold in 1895 for $.85 a keg, and in 1896 for $3.05. In reality, while an ordinary bill of nails would have cost on May 1, 1896, at least $1.70 per keg more than a year earlier, it would not have cost three times as much. No nails were sold at the nominal base price in 1896; and though 60-d. nails were nominally sold at the base rate before the change of card in 1895, the statement that the price of 60-d. nails was at one time $.85 gives a false impression, for reasons which I have explained. A comparison of base prices after December 1, 1896, with earlier ones is altogether misleading, because the present extras are much smaller. It has been estimated that a well-assorted order of nails would carry an average extra of about $.62 on the old card, $.70 on that of July 19, 1895, and $.12 on that of December 1, 1896.[1] Perhaps there is no better simple measure of the actual course of the market than the change in the price of 8-d. nails. This size is used in large quantities; and when assorted orders were required, the extra on it was the same as the required average of extras. But this does not give a perfectly true idea of the changes of price. It is necessary to remember that during the life of the association the prices of the larger nails were increased even more by the increase of the extras on them.

The diagram printed below shows the movement during 1895 and 1896 of the prices of 8-d. wire nails, of No. 11 wire, from which these nails are made, of wire rods and of steel billets. It is based upon the Pittsburg quotations, as published from week to week in the *Iron Age*. No. 11 wire costs about $.10 per cwt. more than the base sizes quoted in the market reports.

Iron and steel went through a notable boom and collapse in 1895. Without any marked change in the general condition of the country, without any corresponding change in general prices, without any strong parallel movement in other countries, the prices of crude iron and steel, and other prices directly dependent on them, rose fast and steadily for some five months, and fell even faster in the next three. Between April 1 and September

[1] *Iron Age*, Dec. 10, 1896, p. 1161.

15 steel billets rose more than sixty per cent, while by December 15 they were within ten per cent of the old level. It is not easy



to get a fully satisfactory explanation of the rise. Near the end of March the Carnegie interests contributed to start it by very

large purchases of iron. About the same time the H. C. Frick Coke Company announced an advance of fifteen per cent in wages, and an advance of more than thirty per cent in the price of coke, to take effect April 1;[1] and other coke shippers followed their lead. This made a great increase in the cost of producing and working iron and steel. A little later labor disputes threatened to stop production; and when they were settled, it was by an advance of wages. Other advances were announced by the great steel companies during May and June. These increases seemed to justify and to fasten the higher prices. Men gathered confidence that good times were coming, and that prices were not only to stay up, but to go higher. This confidence, reacting, bred demand; and renewed demand pushed prices higher and higher. The success of the nail combination, and the temporary activity which the advance in nails and the expectation of advance occasioned in the market, were among the causes which contributed to these phenomena. It is doubtful whether the rise of raw material had the slightest influence upon the price of nails; for the rise of nails began before that of steel, was eminently artificial, and was continued after the raw material had sunk nearly to its former price.

III. The Interests of Dealers and Laborers

The undesirability, from the standpoint of those who want to use nails, of any restriction upon the use of them and of having to pay high prices to get them, is too obvious to be insisted on. The retail hardware dealers suffered with the consumers. Their sales were curtailed, without a proportionate increase in their profit per pound. They had to bear the brunt of their customers' complaints about the price of nails. They complained, also, of the annoyance which was caused by the new card of extras, under which the cheapest nails cost fifty cents per keg more than the nominal base price. When their customers saw nails quoted in the papers at $2.25, it was hard to convince them that the actual wholesale price of 60-d. spikes

[1] *Iron Age*, March 21, 1895, p. 607.

was $2.75. The jobbers, on the other hand, made large profits on the stocks which they bought before the pool was formed, or soon after; and they were enabled, by the system of discounts and rebates, which the manufacturers maintained, to make at least their usual profit on current purchases. This policy was meant to make the jobbers friendly to the association; and it seems to have been largely successful.

Some of the mills showed a disposition to raise wages as they advanced their prices, and so to make some little division of profits with their men. It was reported that one of the great companies gave its men an advance of ten per cent in June, 1895,[1] and ten per cent more about March 1, 1896;[2] that another raised wages ten per cent in July, 1895;[3] and that a third, after a strike, in September, 1895, advanced its wire-drawers ten per cent and fifteen per cent, and its nail-makers five per cent.[4] But the last-mentioned company, which at its full capacity employs about one thousand hands, at one time cut down its force to about three hundred. This reduction is proportional to the reduction of total sales from 500,000 kegs a month to 150,000. It seems safe to assume that the other companies must have made similar reductions. If half or two-thirds of the laborers were thus thrown out of work, they were not much helped by a small increase in the rate of wages paid to the rest.

The restriction of the employment of labor did not stop at the nail mills; there was a diffused effect which was probably greater, though it is less traceable. There is reason to believe that building, and especially repairing, were perceptibly retarded.[5] To raise the retail price of a keg of nails, say from two dollars to four, must under any circumstances diminish purchases to some extent. The effect will be greater if the circumstances make it seem likely that the rise is temporary. In the present case, there was the added influence of a lively conviction of the buyers that the manufacturers were trying to rob them. If a man thinks that an effort is made to impose upon him, he

[1] *Iron Age*, June 20, 1895, p. 1288.
[2] *Ibid.*, March 12, 1896, p. 656.
[3] *Ibid.*, July 18, 1895, p. 129.
[4] *Ibid.*, Sept. 5, 1895, p. 496.
[5] *Ibid.*, June 25, 1896, pp. 1490–1493.

will often subject himself to a good deal of inconvenience, for the satisfaction of thinking that he has not been imposed on. It is likely that thousands of men did without improvements which they could not afford to do without, because they would not submit to what they regarded as the arbitrary demands of the nail combination. It was, perhaps, in part because the manufacturers left this moral effect out of their reckoning, that the extent of the diminution of demand took them by surprise. Their calculations doubtless accorded with the view recently expressed by a small manufacturer, who experienced a strong demand while the association lasted, because he sold nails a little under the association price. He said:

I do not think that the high price of nails restricted consumption to any perceptible extent. The item of nails in the cost of building is a very small one, and it was not over five or six years ago that the price was about the same as that fixed by the recent combination.

Consumption was not so small as production during the last months of 1895, or perhaps during the early months of 1896, while the jobbers still had some part of the stocks which they had laid in about the time the pool was formed. But the best information obtainable makes it appear that, during 1896, consumption as well as production must have been small beyond any possible expectation.

IV. The Interest of the Manufacturers

It is apparently the general opinion that, quite aside from any consideration of the public welfare, and looking only to the pecuniary interest of the manufacturers, the combination carried the policy of high prices too far. The association went to pieces after eighteen months, and prices went down to their former level; therefore it is assumed that the combination failed or, at least, that it would have accomplished its purpose more fully by a more moderate policy. The matter does not seem to me so simple. Mr. Parks, who was undoubtedly the guiding spirit in the whole transaction, went into it with eyes very wide open. He had already been connected with several tack combinations managed on the same principles. Of course they came

to a rather speedy end; but Mr. Parks seems to have counted their experience as favorable, on the whole, to the policy of a short life and a merry one for pools. Moreover, he still maintains the wisdom of the course that he counselled. When the association collapsed, he said that it had lived longer than its most sanguine promoters expected, and as a financial undertaking had been an unprecedented success.[1] The manner of argument of a man who was connected with the association throughout its existence is as follows:

> Suppose we had put up the price $.15 a keg. A great many men who had had their eye on the nail business, would have said: "Those men have put up the price $.15, and they will probably make it $.25. There is going to be money in the nail business. I will go in." But when we put up the price $1.50, they said: "Those fellows are lunatics. They can't hold together. There will be a smash before they get fairly started. I will keep out of that business." As a matter of fact, we had hardly any new competition during the first year of the association. The new competition came mostly after the beginning of the second year. Then men began to say: "Those fellows have kept together twelve months, and they will probably do it a while longer. They are making a lot of money. I will try to get a slice of it." I am sure we kept the association going longer with a high price than we could have kept it going with a low price. I don't believe it would have lasted six months with a raise of $.25. The high price frightened off some people, and gave us plenty of money to buy off the rest.

It is hardly possible to over-emphasize the distinction between the great consolidations of which the so-called sugar trust may be taken as a type—consolidations which it may not be improper to distinguish specifically as trusts, because the typical examples were first united under the proper trust form of organization—and pools like the nail association. The broad differences of organization have their root partly in the conditions of the businesses concerned, and partly, it may be, in the mental characteristics of the managers; and they issue in great differences of policy and power. It would probably not be impossible to bring the making of wire nails under the control of one great company; but it would be much more difficult than it was to do the like

[1] *Iron Age*, Dec. 3, 1896, p. 1108.

with the refining of sugar. To refine sugar by methods commercially practicable to-day, a man must have hundreds of thousands of dollars to put at the risk of the business. With ten thousand dollars and six weeks' time, however, any man who likes can become a manufacturer of wire nails. A little factory can make them, not quite so cheaply as the great establishments which make their own wire, but at no very great disadvantage. It needs only a small rise above the lowest price at which the best mills can pay interest on the cost of their plants, to enable an indefinite number of small mills to start, making each its twenty-five or fifty kegs per day. This is the weakness of any form of combination in a business of this character — the possibility of a new factory in every thriving town.

No limit can be named to the success of skilful and determined managers of a centralized combination or trust, in any line, in crushing competition. An abnormal lowering of price in the local field of a small competitor is a weapon which needs nothing but persistence to make it inevitably fatal to him; and the revenues which the trust draws constantly from other fields, even if it loses in the region of cut prices, give it an unlimited power of persistence. There is no doubt of the trust's ability to destroy any competitor of a size which does not approach its own. This process is troublesome, however, and somewhat expensive; and in a case in which new competitors can spring up with so little money and in so short a time, the query is whether the situation of the trust would not be unpleasantly like that of a man fighting with mosquitoes.

It probably would be so, unless the trust should be content with a policy of greater moderation in its profits than any trust has yet had the self-denial to adopt. Any trust, having once got control of the market, could make it impossible for any competitor to establish a business which would pay a profit for a day, or would need any attention from the trust to make it disappear. This possibility depends upon the power of the trust to do for society such service as no competitor could do. The representatives of the trusts have not been negligent in setting forth the economies which they are able to effect: the production of all goods by the most efficient plants; the uni-

versal use of all improvements, patented or not; the economizing and full use of expert knowledge; the incorporation of subsidiary industries, like the making of packages; the saving of transportation by shipping from the factory nearest the consumer. Greatest of all, perhaps, and most decisive, because it is the economy that is absolutely out of the reach of a competitor, is the commercial economy that depends upon the control of the market — the saving of the expense of inducing customers to buy of this concern and not of that. A trust which should make over the greater part of these savings to its customers, and should content itself with prices which would give it only fifteen or twenty per cent per annum on the value of its productive property, as measured by the cost of replacing it, would probably never be troubled with any shadow of competition. But the general conclusion of competent and disinterested investigators seems to be that, up to the present time, every trust, when its control of the market has been established, has not only kept the whole of the savings of consolidation to itself, but has taken from the public something besides, making prices somewhat higher than they would have been under full competition.

The form of organization of a pool is less unattractive than that of a full consolidation, to a man who values his independent position and dislikes to become an employee; but there is in it as much less power as there is less unity. Under a pool, the economy of closing some establishments may be effected by paying them a bonus, as was done for years by the steel-rail pool. The nail men dealt with outside mills by this plan, but under circumstances and in a way which hardly permit it to be regarded as an economy. It is probable that a pool, with production strictly limited to what the market will easily absorb at the prices fixed, might make some saving in the commercial expenses of advertising and selling, particularly if the circumstances and the policy of the pool were such as to give it a character of comparative permanence. The nail men were probably not able to make any savings of this class. The other economies which are possible to a trust seem to be out of the reach of a pool, while the central organization and the

system of mutual watching seem even to add something to the cost of superintendence. It is probably safe to say that nearly all the gain which any manufacturers may make through a pool is made by raising their selling prices.

It can be maintained with a good show of reason that the nail men would have got more profit in the course of years from the policy of full consolidation, with prices permanently fixed low enough to make competition impossible. But experience has not yet shown this policy to be practically attainable in our present stage of civilization. Between that extreme and the other, which the nail men chose, it is doubtful whether there is any mean which they would have found golden. The choice practically open to them appears to have lain between a tolerably large profit, which might possibly last two or three years, and a very large one, which might be expected to last six months or a year. They chose the very large one; and they kept it, or at least kept the price up, for eighteen months. It is true that a very large part of the profits, especially in the later months, was consumed in subsidies and other expenses of the association. Some well-informed men, intimately connected with the trade and friendly to the manufacturers, think that their policy was short-sighted. The question has more sides than one, however, and it seems possible to make out a very good case for the view that the manufacturers did not choose the least profitable course.

V. The Interest of the Public

It may not make much difference to the manufacturer whether he reduces his costs or raises his selling price; but it makes a great difference to the consumer. Aside from any lowering of prices, it is to the public interest that economies be made — that a given product be obtained with less cost and less exertion. If a consolidated trust would sell as cheaply as competing producers would have to sell, keeping to itself the whole of its economies but taking nothing more, the economies would benefit the public somewhat in the end. The production of wealth and the sum of capital are certainly increased by them; and such increase of

capital and of production tends in itself to the general good. The actual policy of the trusts, in taking from the public something in higher prices besides their gain through saving, complicates the question; but there is a very considerable gulf between the effects of a trust, like the American Sugar Refining Co., and the effects of a pool, like the Nail association. The actual lessening of the human effort that is required for a given result does accompany the trust, and we all are privileged at least to cherish the pious hope that some small fraction of the gain may ultimately work its way around to us. The pool, on the other hand, does not effect any saving of human effort. Its avowed purpose is to increase its members' share of the products of such effort. Its form of organization is probably incapable of producing the greater part of the social benefits which the trusts lay claim to; and it does not make much pretence of trying to produce them.

The claim of the trusts to a socially desirable effect on price takes two forms — that they make prices lower and that they make them steadier. The former effect has probably not appeared permanently in any instance; and the latter does not seem to have appeared generally. Both effects are, however, within their power. Unsteadiness of price, so far as it results from the action of trusts which have once established their control of the market, is generally the result of high prices. The raising of prices above the competitive level causes competition to develop; and competition can be dislodged only by buying it out or by sinking prices below the competitive level. The trusts are regarded by their managers as permanent institutions, and they tend toward the policy which the managers think likely to bring the greatest net revenue in the long run. They tend toward a comparatively moderate forcing of present profits, with a fair degree of attention to the future. In consequence, if the prices of their goods are not steadier than they would be under full competition, they are probably not much less steady. The nail pool, on the other hand, was an ephemeral thing, designed for a quick rush into the market, a grasping of whatever gains might be within reach, and then — collapse. Its purpose was that of a corner — to get the greatest possible amount of profit out of those who had to have nails within a limited time. Its

effect, therefore, was a great exaggeration of the normal unsteadiness of prices.

Too great productive capacity is one of the reasons which are regularly given for forming combinations. The providing of machinery for making far more goods than are demanded at the necessary prices is one of the wastes of competition. Of course it would not be practicable, with the completest centralization, to keep the nominal capacity of machinery down to the actual demand; for variations in the quantities demanded, variations in the kinds demanded, the necessity of being able to make many kinds at each of several places — all forbid an exact adjustment. There is no doubt, however, that here a trust can effect a saving over competitive methods, though it may nullify this benefit more or less completely by stimulating new competition through too high prices. The policy of the nail pool, on the other hand, greatly stimulated the tendency to the overproduction of machinery. The association tried to check it by subsidies to machinery-makers, but with only partial success. Such makers of nail machinery as would accept orders were overwhelmed with them. It was said that persons anxious to get into the nail business "overbid each other, and lucky buyers of machines were offered premiums for their bargains."[1] When the pool collapsed, the machines which the artificially stimulated demand had called forth became, for the most part, dead property. Both to the owners and to society, they are an almost entire waste of capital.

In this way the pool aggravated one of the fundamental difficulties of the situation which it was formed to change. This is, perhaps, its most visibly lasting effect, and from it a serious obstacle arises in the way of renewing the pool. So far as their current business is concerned, the manufacturers might have been in no very different position if the pool had not been formed. The price of nails is now about the same, allowing for the change of extras, as in the spring of 1895. Of the hundreds of new machines which were set up during the eighteen months of fever, a large part have ceased to turn out nails, and as the months go by, others will cease. Some of the older

[1] *Iron Age*, Dec. 10, 1896, p. 1147.

and less efficient will go, one by one, to the scrap pile, and some of the newer may replace them. With the continued progress of invention the rest will doubtless grow relatively less and less efficient. The growth of the country, too, will make a fixed number of machines continually less important as a possible factor in the market. These, however, are processes of years. For a long time to come the hundreds of machines which stand ready to start at a week's notice must be reckoned with by any new combination. A small manufacturer, who was not in the pool, wrote in February, 1897: "I doubt if there will be another combine for a year, but I think it will ultimately come." It will come, as surely as seedtime and harvest; but not in one year, nor, in all probability, in two. It will probably not be possible, until several years have gone by, to form another association which shall effectively control the market.

VI. Conclusions

Only two rather small classes are probably ready to give thanks for the concentrations of industrial and social power which are loosely covered by the name of trusts — those who draw wealth and power from them, and those who, desiring a general absorption of the control of production by society, think that the trusts are forwarding their aim; and some of the former class perhaps would not give thanks without certain haltings of conscience, while many of the latter account the case as one of those in which God makes the wrath of man to praise him. But an unfavorable judgment of the economic and social effects of an institution does not at all involve an unfavorable ethical judgment of the men who visibly represent it — at least in comparison with the rest of the community. The members of the Nail association did what the rest of us would have done in their places. One who was active in forming the association gives this statement of their point of view:

> There is nail machinery enough in this country to produce four times as many nails as can be sold. When there is no pool the makers simply cut each other's throats. Some people think there is something wicked

> about pools. When we were trying to get up the nail pool, I talked with directors of companies who held up their hands against going into any sort of combination. I said to them, "How much did you make last year?" "Not a cent." "Are you making anything now?" "No." "Well, what do you propose to do? Sit here and lose what capital you have got in the business?" Some of them thought they could run along until some of the weak concerns died off. But I tell you plants don't die. If a concern fails, they reorganize it. They buy in the plant cheap, they have got rid of the old debts, and they are in better shape to compete than ever. There is only one way to make any money in a business like the nail business, and that is to have a pool.

This is the aspect that things would wear to us if we were in the position of the manufacturers. Some of us are perhaps opposed to combinations; but so were some that went into the nail pool. In weighing any man's opposition to combinations, it may be doubted whether it is of the sort to keep him out of them, till he has sailed the strait between failing profits and the trust, and has passed the siren voice.

The trusts simply do, with larger resources and higher organization, the things that every manager of a competitive business is trying to do. It is possible that we see the character of such things better when they are done on the larger scale; it may be one of the missions of the trusts to give us clearer and higher notions of ethics. But it seems probable that, if we begin to cast stones, the houses of the trusts will not be the only ones to suffer. If it is asserted to be wrong to crowd up the prices of the things we sell and to crowd down the prices of things we buy, wrong to make our business large by the destruction of our neighbor's, a good deal may be said for the ethical superiority of the altruistic man who should refuse to do these things; but no ethical distinction can be drawn between the man who does them strongly and successfully and the man who is only able to do them with less strength and less success.

The mechanism of the trust, properly so called, is perhaps not unworthy to be ranked among the greatest inventions of this century, either as a monument of intellectual acuteness or as an engine of momentous social effects. Like most of those other inventions which are more unanimously classed as useful,

and for which individuals get credit, the invention of the trusts did not really depend on the activity of any particular men. If neither Bell, nor Reis, nor McDonough, nor Edison had lived, a score of other men were looking for the telephone, and would soon have discovered it. Scientific and technical knowledge had reached a point from which it could not but be discovered; and no man could do more than hasten the discovery by a little. Just so, the development of the pool, the trust, and the giant consolidated corporation was inevitable in the social and economic conditions of our age. If the world had lacked Mr. Rockefeller and his associates, it had other men of business and other lawyers; and it would not long have lacked the trust.

CHARLES E. EDGERTON

OTHER IRON AND STEEL POOLS[1]

The Steel-Rail Pool.[1] — By far the most important pool organization in the steel industry at this time was that in steel rails. This pool was formed on August 2, 1887, and, while it was dissolved in 1893, it was speedily renewed and continued in existence until the early part of 1897. The general nature of this pool may perhaps best be indicated by reproducing the following copy of the memorandum of agreement:

Memorandum of agreement, entered into August 2, 1887, *by and between the North Chicago Rolling Mill Company, the Cambria Iron Company, the Pennsylvania Steel Company, etc., etc.*

We, the before-named companies and corporations, manufacturers of steel rails, hereby mutually agree one with the other, that we will restrict our sales and the product of steel rails of 50 pounds to the yard and upward, applying to orders taken by us and to be delivered by us or from our respective works during the year 1888, as hereinafter

[1] U. S. Bureau of Corporations, Report on Steel Industry, July 1, 1911, pp. 69–74; Stevens, *op. cit.*; the Stanley Committee Congressional Investigation Hearings, 62nd Cong., 2d sess., 1911–12; and *U. S.* v. *U. S. Steel Corporation*, Statement of the Case, pp. 260–343; give more details. On the so-called "Gary dinners," details are given in the next chapter, p. 178 *et seq.*

allotted and limited; and we respectively bind ourselves not to sell in excess of our current allotments, without first obtaining the consent of the Board of Control thereto — that is to say:

It is agreed, there shall now be made an allotment of 800,000 tons of rails, which shall be divided and apportioned to and among the several parties hereto to be sold by them during the year 1888, upon the following basis of percentages, to wit: North Chicago Rolling Mill Company, $12\frac{1}{2}$ per cent; Pennsylvania Steel Company, $9\frac{8}{10}$ per cent; etc., etc.

And in addition to the said allotment of 800,000 tons of rails above allotted, an additional allotment of 250,000 tons is hereby made and allotted to the Board of Control, to be reallotted and reapportioned by it, as and to whom it may deem equitable, in the adjustment of any differences that may arise. It being also further agreed that all subsequent allotments of rails hereafter made, to be sold under this agreement during the year 1888, shall also be divided and apportioned to the several parties hereto in the same ratio of percentages as said apportionment of 800,000 tons is herein divided and apportioned.

It is further agreed, that the Board of Control shall, from time to time, make such further allotments as shall be necessary to at all times keep the unsold allotments at least 200,000 tons in excess of the total current sales, as shown by the monthly reports of sales. This is to be in addition to the then unappropriated part of the 250,000 tons hereinbefore alloted to the Board of Control to adjust differences.

It is further agreed, on the first day of April, July and October, the Board of Control are authorized and directed to cancel such part of the unmade allotments of the respective parties hereto as they the said Board of Control shall determine such party unable to make in due time, and all allotments so canceled the Board of Control shall have the right to reallot to any of the other parties hereto; it being understood that all such cancellations shall apply only to allotments standing to the credit of the respective parties hereto on the dates above named, but no reallotment as aforesaid shall be made by the Board of Control to any of the parties hereto for the purpose of enabling them, or any of them, to make and sell rails from foreign made blooms.

It is further agreed, that all transfers of parts of allotments from one party to another shall be made by the Board of Control.

It is further agreed, that there shall be a Board of Control, consisting of three members, namely, Orrin W. Potter, Luther S. Bent and

W. W. Thurston, who shall have power to employ a paid secretary and treasurer.

It is further agreed, that the Board of Control, upon the written consent of 75 per cent of the percentages as hereinbefore named, shall increase the allotments for the year 1888, and such increase shall be allotted to the parties hereto as hereinbefore provided.

It is further agreed, that each party whose name is hereunto annexed, shall and will make monthly returns to the Board of Control of all contracts for delivery of rails of 50 pounds to the yard and upward during the year 1888, and also of all shipments of such rails made by them during said year; a copy of such return shall be furnished to each party hereto.

It is further agreed, that all the parties hereto shall and will, on or before January 15, 1888, make a written return to the Board of Control of all rails of 50 pounds to the yard and upward (designating the weight) which they respectively had on hand January 1, 1888, stating whether the same are sold, and if sold, on what order they apply.

It is further agreed, that the Board of Control shall have the right whenever they deem it expedient to convene a meeting of the parties hereto, and they shall give at least 10 days' previous notice of all meetings, and any business transacted at such meetings, and receiving 75 per cent of the votes present thereat, either in person or by proxy, shall be binding on all the parties hereto, excepting as to a change in percentages as aforesaid.

The Board of Control shall be required to call a meeting of the parties hereto when requested so to do in writing, signed by any three of the contracting parties, but such request and such notice shall state the object for which such meeting is called.

It shall be the duty of the Board of Control to have a proper record kept of all the returns made to it, with power from time to time to change the form of return as they may deem expedient.

The Board of Control shall have authority to levy an assessment, pro rata to the allotted tonnage, to defray the actual expenses made necessary to carry out this agreement.

It is further agreed, that we will, respectively, immediately make return to the Board of Control of all rails of 50 pounds to the yard and upward which we are now under contract to deliver during the year 1888, said return to state to whom such rails are sold and when they are to be delivered.

North Chicago Rolling Mill Company, by O. W. Potter, president; Cambria Iron Company, by E. Y. Townsend, president; etc., etc.

This agreement, it will be seen, was designed to provide a very effective control of the production of steel rails by members of the pool, who together manufactured at that time more than 90 per cent of the country's output.

The distinguishing characteristics of the rail pool were a fairly compact organization and the inclusion of nearly all rail manufacturers, while the rather extensive plant necessary for the production of rails tended to discourage new competition. The bulk of railroad purchases of steel rails, moreover, are usually made once a year. These conditions favored the maintenance of pool prices and probably explain the stability of this pool as compared with others in the iron and steel industry at this period.

However, the rail pool was by no means completely successful. Despite its fairly compact organization, it collapsed in the latter part of 1893 as a result of disagreements over the allotment of tonnage, aggravated by the commercial depression of that year. In 1894, after numerous conferences, it was reorganized, but the slack demand of 1896 resulted in new infractions of the agreement, as a result of which the pool collapsed in February, 1897. This second disruption of the pool was followed by a brief but exceedingly bitter price war, during which sales of steel rails were made freely at prices ranging from $20 to $15 per ton. The nominal pool price of rails had for some time been $28.

The Steel-billet Pool.—This pool was formed in April, 1896, under the name of "The Bessemer Steel Association of the United States." The agreement, which was along the same lines as that of the steel-rail pool, provided for a definite allotment of tonnage among the members, the maintenance of prices, the payment of penalties for exceeding the tonnage allotments, and compensation, on the other hand, to those members who did not make the maximum production to which they were entitled.

The billet pool had a stormy existence from the start. This was due partly to the fact that it failed to include several important manufacturers of billets, but more particularly to internal dissensions. An especial source of weakness was that

while some of its members made nothing but the cruder steel products, such as billets, slabs, etc., and were therefore dependent upon the outside market, several of the larger concerns in the pool had their own finishing mills, which thus afforded them an outlet for a large quantity of their semifinished steel. The agreement as originally drawn up did not cover billets thus used by pool members themselves in the manufacture of finished products. As a result, such concerns took advantage of the situation by entering into heavy sales of finished material, and at prices so low that outside finishing mills were unable to compete and at the same time pay the pool price of billets. Consequently there was a heavy reduction in the trade demand for billets, and those members of the pool who were dependent upon this outside demand naturally became intensely dissatisfied. As a result of these conditions, the pool was apparently on the point of disruption during the summer and fall of 1896. In November the arrangement was amended by including in the tonnage allotment steel used by pool members in the manufacture of finished material as well as that sold in the cruder forms. This change, however, had hardly been accomplished when fresh difficulties arose over alleged bad faith of some of the members. In the first week of December, 1896, one member of the pool, the Bellaire Steel Company, formally announced its withdrawal. This action was promptly followed by the collapse of this pool.

The Ore Pool.—This pool, which was called the Bessemer Ore Association, embraced the leading ore-producing interests in the Lake Superior region. The keen competition which ordinarily exists in a mining business where ownership of ore properties is scattered was intensified by the commercial panic of 1893, and profits, for many mining concerns, had practically disappeared. The pool agreement contemplated a rigid control of the business. Aside from fixing prices for ores, it also undertook to make a definite allotment of production, both as to mining ranges or districts and also as to the individual mining companies included in its membership.

Owing to important changes in the ore industry in 1896, some of which are noted later, the ore pool was threatened with

disruption, and in the spring of 1897 it seemed almost certain that no agreement would be made for the coming season's business. An arrangement was nevertheless entered into by some of the leading producers, but on a very much lower basis as to price. Thus, whereas the standard price for Gogebic ores in 1896 had been $4 a ton, the basis in the 1897 agreement was about $2.75.

IV

THE ADDYSTON PIPE COMPANY[1]

THE relevant facts may be classified under the following headings: first, the terms of the trust agreement; second, its purposes; third, its practical construction and operation; fourth, its effects upon the public.

I. TERMS OF THE AGREEMENT

The six companies are located as follows:

Addyston Co.	Cincinnati, Ohio
Dennis Long & Co.	Louisville, Ky.
South Pittsburg Co.	South Pittsburg, Tenn.
Chattanooga Co.	Chattanooga, Tenn.
Anniston Co.	Anniston, Ala.
Howard Harrison Co.	Bessemer, Ala.

It is to be borne in mind in understanding this agreement that the greater part of the business consists in taking contracts for municipal corporations, gas or water companies, and other large institutions which usually invite bids from various competitors.

The earlier agreement of December 28, 1894, is of present importance only in so far as its provisions have been continued in effect, namely, in respect to the "reserved cities" and to the extent of the "pay territory." The main agreement was proposed by John W. Harrison, President of the Howard Harrison Co., on May 16, 1895, and adopted on May 27, 1895, in the form of a resolution entered upon the minutes of the association. It is as follows (page 83):

[1] From argument of Hon. E. B. Whitney, U. S. Assistant Attorney-General, in *U. S.* v. *Addyston Pipe and Steel Co.*, U. S. Circuit Court of Appeals, Sixth Circuit. Appeal Case No. 498. Page references run to the testimony in the official court record. The opinion in the above case is reprinted in part in Chapter XVI, *infra*.

That from and after the first day of June that all competition on the pipe lettings shall take place among the various pipe shops prior to the said letting. To accomplish this purpose it is proposed that the six competitive shops have a "representative board" located at some central city to whom all inquiries for pipe shall be referred, and said board shall fix the price at which said pipe shall be sold, and bids taken from the respective shops for the privilege of handling the order, and the party securing the order shall have the protection of all the other shops. . . . All division of bonuses to remain as now established during the year 1895.

This system of bidding is known as "buying a job" (page 89).

One exception to the general rule is that of the "reserved cities" which remain tacitly under the resolution of December 28, 1894, as follows (pages 77–78):

Third. The Addyston Pipe and Steel Company shall handle the business of the Gas and Water companies of Cincinnati, Ohio, Covington and Newport, Ky., and pay the bonus hereafter mentioned, and the balance of the parties to this agreement shall bid on such work such reasonable prices as they shall dictate.

Fourth. Dennis Long and Company of Louisville, Ky., shall handle Louisville, Ky., Jeffersonville, Ind., and New Albany, Ind., furnishing all the pipe for Gas and Water works in above named cities.

Fifth. The Anniston Pipe and Foundry Company shall handle Anniston, Ala., and Atlanta, Ga., furnishing all pipe for Gas and Water companies in above named cities.

Sixth. The Chattanooga Foundry and Pipe Works shall handle Chattanooga, Tenn., and New Orleans, La., furnishing all gas and water pipe in the above named cities.

Seventh. The Howard Harrison Iron Company shall handle Bessemer and Birmingham, Ala., and St. Louis, Mo., furnishing all pipe for Gas and Water companies in the above named cities; extra bonus to be put on East St. Louis and Madison, Ill., so as to protect the prices named for St. Louis, Mo.

Eighth. South Pittsburg Pipe Works shall handle Omaha, Neb., on all sizes required by that city during the year of 1895, conferring with the other companies and coöperating with them; thereafter they shall handle the Gas and Water companies of Omaha, Neb., on such sizes as they make.

NOTE.—It is understood that all the shops who are members of this association shall handle the business of the gas and water companies of the cities set apart for them including all sizes of pipe made by them.

A modification was made, however, on December 19, 1895, as follows (page 84):

That upon all inquiries from prices from "reserved cities" for pipe required during the year of 1896, that prices and bonus shall be fixed at a regular or called meeting of the principals.

Another exception recognized was that of "special customers" of the different concerns. As to these it was resolved on May 27, 1895 (page 84):

That when an inquiry is reported to which a member can properly establish a claim as a special customer, such inquiry should not be disposed of by the "auction basis," but shall be handled by such member, the committee fixing the price and bonus, such price and bonus to be commensurate with prices and bonuses at the time such inquiry shall be reported.

It was further resolved on the same day (page 84):

That all parties to this association having quotations out shall notify their customers that the same will be withdrawn by June 1, 1895, if not previously accepted, and upon all business accepted on or after June 1st, bonuses shall be fixed by the committee.

The provisions of this agreement operated only in what was called the "pay territory" or "bonus territory." This territory is described in the pleadings, the opinion of Judge Clark, and the resolution at page 78 of the record. It includes the whole of the United States except Virginia and the States north and east thereof, and except the Territory of Alaska.

The bonuses, when not fixed on the "auction basis," are fixed by a schedule shown on page 78, by such modifications as have since been made therein, or by special order of the committee.

To carry out the objects of the association, headquarters were established at Cincinnati, Ohio, with an office force and a committee of representatives from the various shops (pages 83–84). The bonuses, after December 20, 1895, were divided according to a schedule based on the following estimated tonnage of the various shops (page 86):

	Tons
South Pittsburg	15,000
Anniston	30,000
Chattanooga	40,000
Bessemer	45,000
Louisville	45,000
Cincinnati	45,000

The bonuses were not paid upon the acceptance of the bid or even upon the successful closing of the contract with the purchaser, but only upon the actual shipment of the pipe. Thus the schedule last quoted reads as follows (page 86):

1st. On the first 90,000 tons of pipe *shipped* into "pay territory" 16" and smaller sizes shall be divided among the six shops [etc.].

In order to insure the proper working of the combination, an auditor's office was established and regular reports required. Thus (pages 80–82):

Third, Sec. 1st. Each shop shall report daily to the auditor all orders secured in bonus or free territory, giving the shop number [etc.].

Sec. 2d. On the 1st and 16th of each month they shall report to the auditor all *shipments* made in all territory, giving shop number [etc.]; showing the amount of bonus and tonnage, of the bonus as well as free territory.

Sec. 4th. The auditor shall make carbon copies daily of all reports received, and send one to each shop, and to such others as may be designated.

* * * * * * * *

Sec. 3d. He shall on the 1st and 16th of each month, or as soon as practicable, send to each shop a statement of all shipments reported in the previous half months, with a balance sheet showing the total amount of the premiums on *shipments*, the division of the same, and a debit credit balance of each company; also a statement of free orders secured during the same period; and a memorandum of balance payable from one to another.

* * * * * * * *

Whoever has a representative at any public letting shall instruct him to send to the auditor a full list of the bids and bidders on same; also that all information in regard to work taken in pay territory by the shops outside of this association shall be reported to the auditor, who shall

keep a proper record of such information and send carbon copies of same to all of the members of this association.

* * * * * * * *

That whenever an order is reported by any shop, and a doubt exists as to the proper bonus to be paid, that it be reported with the facts in the case, to be acted upon at the next meeting of the executive committee.

The combination also kept a "black list" for some boycotting purpose not explained (page 90).

* * * * * * * *

2. Purposes of the Agreement

The agreement of May 27, 1895, contains the following recital of its purpose (pages 82–83):

Whereas, the system now in operation in this association of having a "fixed bonus on the several States" has not in its operation resulted in the *advancement in the prices of pipe* as was anticipated, *except in "reserved cities,"* and some further action is imperatively necessary in order to accomplish *the ends for which this association was formed:* Therefore [etc.]

Mr. Bowron of the South Pittsburg company says that the association was established "to maintain fair prices and a just distribution of work" — "to maintain fair prices and secure for each a fair proportion of the work in a certain territory, by restraining in a certain measure competition as among themselves only" — "to restrain competition as among defendants and allow to each a profitable division of work according to its relative capacity, and thereby maintain fair prices to all" (pages 194–195).

Mr. C. W. Harrison of the same company says that it was "on the theory that destructive competition results in monopoly," and that it "was the purpose of this association to maintain fair prices and secure for each of its members a fair proportion of the work in a certain territory by restraining in a reasonable measure competition as among themselves only" (page 216).

Mr. Callahan of the Louisville company says that it was "to maintain fair prices, to regulate credits, and to accomplish an

equitable distribution of such orders as the six defendants could secure in competition with the other manufacturers of cast iron pipe" — "by regulating to a certain extent the competition among the defendants only, to endeavor to maintain fair prices, and to secure to each of the defendants a fair proportion of the orders in a certain territory" (pages 263–264).

In describing the auction system, Mr. Callahan clearly states what "fair prices" mean as understood by such combinations: "These voluntary offers from defendants were each based upon such prices for the respective orders as these defendants considered would be fair and reasonable prices" (page 264).

That fairness and reasonableness from the consumers' point of view was not at all taken into consideration is shown by the prices actually charged in "pay territory" as set forth in the record, and by a letter of Mr. Thomasson of the Chattanooga company (pages 102–103):

> We believe that as a general thing we have had our prices entirely too high, and especially do we believe this has been the case as to prices in "reserved cities." The prices made at St. Louis and Atlanta are entirely out of all reason, and the result has been and always will be, when high prices are named, to create a bad feeling and an agitation against the "Combination." There is no reason why Atlanta, New Orleans, St. Louis, or Omaha should be made to pay higher prices for their pipe than any other places near them who do not use anything like the amount of pipe and whose trade is not as desirable for many other reasons.

The affidavits of defendants show how in some respects this combination works beneficially by distributing orders in such a manner that a greater regularity of employment is obtained at the different shops. This is immaterial. Probably few unlawful combinations would fail to secure economy of service to some considerable extent. The element of evil does not fail to vitiate the agreement because it contains likewise an element of good. A most interesting letter of Mr. Thomasson (pages 110–112) shows that the bonus system was not intended to work, and did not actually work, simply as a distributor of employment, leaving the price charged to the consumer merely the actual cost with a fair business profit. While some proportion of the bonus may

represent economy in production, a part of it is shown to represent an extra profit divided up among the different companies. Mr. Thomasson points out how the Bessemer company is going too far in speculating on this extra profit, and how his own company is secretly taking advantage of this error of its associate (page 111):

If they should continue to buy all the pipe that goes up to such figures as they have paid for Jacksonville and other points, they would wreck their shop in a few months. However, they of course calculate this bonus *will be returned to them on work taken by other shops.* We are very much pleased with the bonus that has been paid, and we only hope they will keep it up as it is only money in our pockets. . . . We note Mr. Thornton's report of average premiums from June 1 to December that the average was $3.63. The average bonuses that are prevailing to-day are $7 to $8. We cannot expect this to continue. . . . If we cannot secure business in "pay territory" at paying prices, we think we will be able to dispose of our output in "free territory," and of course make some profit on that. At the prices that Howard Harrison people paid for Jacksonville, Des Plaines, and one or two other points, they are losing from $2.50 to $3 per ton, that is, provided "bonuses" would not be returned to them. Therefore when business goes at a loss we are willing that the other shops make it. . . .

P.S. — Do not leave this letter on your desk, where it might fall into the hands of others. Make a memorandum and tear the letter up. Above all things make a confidant of no one in business matters.

I shall comment again later on this letter.

3. Practical Construction and Operation

The record gives some interesting information about the working of this agreement in different cities.

Chicago. — At a meeting of the associates on February 14, 1896, it was decided that an order of the Chicago Gas Company should be filled at $22 and $21.50 with a bonus of $5 (page 88), and (apparently on some other Chicago advertisement, page 89):

On motion of A. F. Callahan, it was agreed on the dates of the Chicago letting at least five of the shops should be represented and a majority of them should decide what bid should be made. The job to be regularly disposed of by the committee before the letting.

The presence of five shops at the letting was in pursuance of the system of "protecting bids," by slightly higher false bids on the part of the companies which had agreed with the combination not genuinely to compete for the order. This system has been consistently maintained by the associates. Its advantages for purposes of concealment are obvious.

Louisville. — The record of December 28, 1895, contains the following (page 85):

F. B. Nichols moved that Dennis Long & Company be *allowed* to close contract for the year of 1896, with the Louisville Water Company at the best price they can obtain for same, and after securing contract refer the same to the meeting of the principals to fix bonus.

Seconded by A. F. Callahan. Carried.

St. Louis. — Mr. Nichols of the Bessemer company writes to the other companies on January 24, 1896, as follows (page 94):

I prefer that if any of you find it necessary to put in a bid without going to St. Louis, please bid not less than $27.00 for the pipe, and $2\frac{3}{4}$ cents per pound for the specials. I would also like to know as to which of you would find it convenient to have a representative at the letting. It will be necessary to have two outside bidders.

St. Louis was a "reserved city" belonging to the Bessemer company (page 77), and paying a bonus of $2 per ton (page 78). The amount shipped from April 1, to December 31, 1895, was 10,970 tons, giving a bonus of about $22,000 to the combination (pages 94–95).

Knoxville. — The Knoxville Woollen mills on April 25, 1896, wrote to Chattanooga and Bessemer for quotations of cast iron pipe (page 62). This contract seems to have been bid in by Chattanooga, which telegraphed the other companies on April 29: "We will advance price Knoxville Woollen mills dollar and half; please protect" (page 96), at the same time bidding $22 per ton (page 63). Bessemer accordingly, through Mr. Nichols, bid $22.24 per ton on April 30, with the hypocritical comment, "Trusting that we will be favored with your order, we are yours truly" (pages 63–64).

Omaha. — The working of the agreement is well shown by the bidding for Omaha on December 20, 1895 (page 87):

W. L. Davis moved to sell the 519 pieces of 20" pipe for Omaha, Neb., for $23.40 delivered.

Seconded by D. R. P. Dimmick. Carried.

F. B. Nichols moved that Anniston participate in this bonus and the job be sold over the table.

Seconded by W. L. Davis. Carried.

Pursuant to the motion the 519 pieces of 20" pipe for Omaha was sold to Bessemer at a premium of $8.

The water companies of Omaha belong to South Pittsburg (page 77). The receiver of one of them called for bids in April, 1896, under competitive circumstances which the company's agent evidently thought "will make him some trouble, especially if we try to obtain too high a price" (pages 120–121). In response to a call upon Chattanooga for "protection" Mr. Thomasson wrote as follows on April 28 (page 121):

Please advise us at once as to what figure we shall make on this work. Please do not ask us to make a price of two or three dollars per ton higher than yours, but give us a reasonable price to name.

The Pittsburg company responded (page 122):

We request that you please quote the American Water Works Company of Omaha price of $24.80 per ton of 2000 pounds f. o. b. Omaha.

Accordingly Chattanooga wrote the following candid letter to the Receiver at Omaha (page 122):

Dear Sir: Replying to your favor of the 25th instant, we propose to furnish cast iron pipe as per specifications for $24.80 per ton two thousand pounds, and will furnish special castings from our regular patterns for two and one-fourth cents per pound, all delivered on board cars Omaha, Neb. We are in a position to give you prompt shipment on this pipe *and trust this time we will be favored with your order.*

Very truly, yours,

Chatta. Fdy. & Pipe Works,

By E. B. Thomasson

Such letters may afford the court some hint as to the amount of weight which can be placed upon the testimony of the gentlemen who manage this honest combination.

Atlanta. — This city was the property of the Anniston company (page 77), which paid a bonus of $2 per ton as the rent of the

property (page 78), until it was provided that such bonuses should be fixed at a meeting of the principals (page 84). On February 15, 1896, the Chattanooga company had an inquiry from the Atlanta Water Works for 1500 feet of 12″ pipe, and about 12,000 feet of pipe varying from 6″ to 10″ with a lot of special castings. The company, through Mr. Thomasson, at once asked Anniston "As to what price you desire us to protect on this contract" (page 97). Anniston answered through Mr. Dimmick (page 97):

> Please protect $24 on approximately 375 tons of cast-iron pipe for the city of Atlanta, Ga., on which we are asked to-day for prices. We have sent a man over to Atlanta and will get as much more as possible.

This price was nearly $10 per ton (less cost of transportation) over what would be a paying profit at Chattanooga (page 111). Chattanooga, however, bid $24.50 per ton delivered on board cars at Atlanta, adding with its usual ingenuousness: "We can give you a prompt delivery on above pipe and would be pleased to receive your order" (page 98). A lower bid had been received from R. D. Wood & Co., of Philadelphia, but all bids were rejected by the Atlanta people, as they "were extremely high" (page 98). The bids thus rejected give a good example of the method by which these companies "protected" each other, and incidentally led the consumer to suppose the prices reasonable. They were: Anniston, $24; Bessemer, $24.25; South Pittsburg, $24.25; Chattanooga, $24.50 (page 53).

Anniston at once telegraphed Chattanooga: "Stand pat on your price" (page 99), and in response to complaints about the high price replied: "We believe we made a mistake in trying to get $24 for pipe and 2½ cents for specials, but there would have been no difficulty in this respect had we not run up against R. D. Wood & Co.'s man there putting in his bid for hydrants, and he also put in a bid for the pipe and specials at the last moment;" that "they [the Atlanta authorities] stated it was their belief that the four southern shops have an arrangement by which Anniston is to get the work; in other words, that we had a combination between us, and if they can find it out positively, they will never receive a bid from any of us again;" and recommended that all four southern shops have representatives on the

ground at the next letting on March 4 (pages 99–100). The Anniston company's report from its agent at Atlanta is given in full at pages 100–101. Besides the Philadelphia man he met Mr. Torbett, Secretary of the Water board, Mr. Erwin, one of the Water Commissioners, and Colonel Woodward, Superintendent of the Water Works. He told the city council that "the ruling market price" would be about $24, and got a favorable resolution through the council without a dissenting vote. The Philadelphia man, however, at the last moment put in a bid of $23. The threat against the four southern shops came from Mr. Erwin, and Colonel Woodward also advised the rejection of all bids. The colonel's advice may have been on the ground that "he promised me when there last he would give us another chance in the event we were not the lowest bidders." In other words, he knew that the Anniston company could afford to furnish the pipe at a lower price than what they were passing off as the "ruling market price." It is not surprising that the colonel appears as an affiant on behalf of the Anniston company, maintaining that its prices were "fair, reasonable, and moderate" (pages 200–202), though perhaps it may be surprising that Mr. Erwin fell in line with him (page 202).

Negotiations were opened with the Philadelphia concern to prevent its appearance at the second bidding (page 103). On April 10 (page 59) the contract was made with the Anniston company at $22.75 for the year's supply, and $22 for some "special shipments." Assuming the cost with a fair profit at Anniston to be substantially the same as at Chattanooga, and assuming the freight from Anniston to Atlanta to be $1.60 per ton (page 90), this made a price of about $6.75 per ton over and above a fair and reasonable profit. This seems to be an underestimate, because we find the following entry in the minutes of the Associated Pipe Works for March 13, 1896 (page 90):

> Moved that "bonus" on Anniston's Atlanta Water Works contract be fixed at $7.10, provided freight is $1.60 a ton. Carried.

Before payment was made by the Atlanta Water Works, an investigation was had, based upon charges by the same man whose information led to the present suit. The charges were

referred to a special committee, consisting of Messrs. Erwin and Torbett and one Hass, on May 18, 1896 (page 203). The city's attorneys had advised that the city could recover in a suit against the Anniston Works (pages 207–210). The committee, however, unanimously overruled the attorneys after hearing the officers of the Anniston company (pages 203–210).

4. The Effects upon the Public

It is not essential to show deleterious effects upon the public, but the subject is an interesting one, and the gleams of light from this record are also interesting.

The defendants have repeated *ad nauseam* affidavits tending to show that there were other large works — larger perhaps than their own — in the United States. A tonnage statement, for instance, is given (by an interested witness and annexed to an evasive affidavit) of factories through the country, including some very large ones in Pennsylvania and New Jersey (page 270).

It also appears, however, that the rates of freight are very high. For instance, pipe which is worth from $13 to $14.75 at the shop in Chattanooga (page 111) pays $6 to Peabody, Mass., and $5.55 to Lockhaven, Pa. (page 104); $5.60 to Clifton, N. Y. (page 105), $4.80 to Wytheville, Va., $5.40 to Troy, N. Y., $3.90 to Allegheny, Pa., and $4.95 to Syracuse, N. Y. (page 106). The effect of these high rates, together with the location of these factories on or near the west slope of the Appalachian mountain range, gives to them (and to the few other western works) a practical monopoly of nearly all the "pay territory"— in other words, of everything but the Northern and the Middle states. To this general statement there must be, of course, an exception as to localities on the coast line and elsewhere within the "pay territory" that are within the reach of northeastern factories. The small importance of these exceptions, however, may be gathered from the affidavits submitted by defendants themselves. They have undertaken to show the actual origin of the pipe used in large portions of the "pay territory," and have only succeeded in identifying the great Pennsylvania and New Jersey factories with two small lots of unspecified amount (pages 213, 271). They

content themselves with such evasive statements as those of Mr. Callahan at page 265 of the record, specifying neither the size of the orders nor the portions of the "pay territory" where they are found.

It is clear that as to the bulk of the "pay territory" — that is, as to the bulk of the United States — their competition comes from but few rivals. In main it seems to be confined to the works at Cleveland, Columbus, and Newcomerstown, Ohio, and Detroit, Mich., whose capacity is 200, 100, 75, and 75 tons per day, respectively (pages 197, 250, 181, 188). A concern is indeed mentioned as competing at St. Louis, but it is suspected to be identical with the Bessemer concern (pages 61–62), with which it is almost identical in name. The factories in Colorado and Oregon are small and seem to cut only a local figure. The same may be said of the Texas penitentiary.

Such information as is given us leads to the conclusion that the Ohio and Michigan concerns have the smaller end of the business, even in territory for which transportation rates permit them to compete. Mr. Hallett, a general contractor in Aurora, Ill., gives the precise figures for his purchases in 1895 and 1896. He purchased 514 tons from the combination, 25 tons from the Newcomerstown concern (J. B. Clow & Son), and 50 tons from jobbers (pages 123–124). Mr. W. H. Garrett, of Batavia, Ill., gives the purchases of the Water Works Department of Fairbanks, Morse & Co. for the same period. They included 1023 tons from the combination, 690 tons from Columbus, 79 tons from Cleveland, and 35 tons from the Glamorgan Pipe and Foundry Co. of Lynchburg, Va. These purchases were "in the business of contracting water works for municipalities *throughout the United States*" (pages 129–130).

We could judge more accurately of the strength of the Associated Pipe Works if we were definitely informed as to their capacity *per diem*. They have been so careful to produce testimony as to the *per diem* capacity of other companies (pages 178–179, 180–181, 187–189, 196–198, 198–200, 249–250) that we may infer that there was good reason for their failing to be specific as to their own. The only specific testimony bearing on the point is that of Mr. Llewellyn as to his Chattanooga company. He gives its

capacity at "about 40,000 tons of cast iron pipe and special castings annually" (page 243). This figure, however, is evidently taken from the minutes of the combination at page 86, which is shown by Mr. Thomasson of his own company not to represent the actual capacity of the various works, but their usual output (page 111). The 40,000 tons ascribed to Chattanooga represent its proportion of the 220,000 which are assumed, not as the full capacity of the works, but as their probable annual shipments into pay territory. The total of these shipments is estimated at 220,000 for the six companies, but Mr. Thomasson says:

> We think a very conservative estimate of shipments into this territory will amount to fully 200,000 this year; more than that — probably overrun 240,000 tons.

The same estimate which gives Chattanooga 40,000 gives South Pittsburg and Anniston 45,000 combined (page 86); but the officers of these companies join with Mr. Llewellyn himself in verifying the answer (pages 43–44), which contains the following statement as to the "pay territory" (page 36):

> They, however, deny that the shipments of pipe for 1896 amount to more than 100,000 tons in said territory, which they aver could have been supplied by any two of defendants so as to deprive all others of any share thereof.

In ascertaining the actual capacity we may therefore pretty safely double the estimate at page 86, and assume it to be 440,000 tons a year, or nearly 1,500 tons per day, as against the 450 tons per day of their four principal rivals.

As confirmatory of the position that no reliance is to be placed upon the statements of these defendants as to the relative working capacity of the different shops (except when their statements are not made for use in the present suit), we may compare the answer which they all join in verifying with the testimony of their own witnesses concerning the capacity of other works. Thus, the answer states the capacity of Scottdale as 200 tons instead of 100; of Columbus as 150 tons instead of 100; and of Detroit as 100 tons instead of 75 (pages 44, 179, 188, 250).

Another example of the misleading character of this testimony is in the statement of Mr. Callahan at page 265 as to the actual

clearance settlements amounting in 1895 to only 38 cents per ton, when compared with Mr. Thomasson's letter of January 2, 1896, showing that the average premiums from June 1 to December 31, 1895, were $3.63 (page 111).

Besides the partial monopoly which they were enabled to maintain through the high transportation rates and the limited output of their western rivals, they doubtless resorted to special means for diverting rivalry, such as the negotiation for the withdrawal of the Philadelphia company from competition at Atlanta (page 103), and the plan to prevent one Drummond "from invading our western territory" (page 113).

Reasonableness of prices. — It will be borne in mind that, even under the common law doctrine permitting reasonable restraints of trade, the burden of proof as to reasonableness is on the defendant.

"Wherever such contract *stat indifferenter*, and, for aught appears, may be either good or bad, the law presumes it *prima facie* to be bad" (Lord Macclesfield in *Mitchel* v. *Reynolds*, *supra*, at page 701). "In all restraints of trade, where nothing more appears, the law presumes them bad" (id., at page 704). "The general rule is that all restraints of trade which the law so much favors, if nothing more appear, are bad" (Willes, C. J., in *Master of Gunmakers* v. *Fell*, Willes, 388). "Contracts in restraint of trade are in themselves, if nothing more appears to shew them reasonable, bad in the eye of the law" (Tindal, C. J., in *Horner* v. *Graves*, 7 Bing., 735, 744; S. P. Patterson on "Contracts in Restraint of Trade," page 5; *Pierce* v. *Fuller*, 8 Mass., 223; *Chappell* v. *Brockway*, 21 Wend., 157, 159; Addison on "Contracts," page 1154).

We have in this record, however, affirmative evidence of the unreasonableness of the profits obtained by these corporations. Their unreasonableness is shown in various ways, such as by adding the price at the factory (page 111) to the transportation rate (page 90), and comparing this with the prices actually obtained, which usually range from about $22 to $25 per ton. It is also shown by the actual bonuses paid to the combination for the privilege of getting a contract, these bonuses running up to such figures

as $7.10 (page 90), $7.50 (page 88), and $8.00 (page 87) — averaging from $7.00 to $8.00 in January, 1896 (page 111). It is also shown by the large amounts of the aggregate bonuses which were divided up among these companies (pages 116–117). It is confirmed by the statement of the Chattanooga company itself that the prices were "entirely too high," especially in the "reserved cities"; that "the prices made at St. Louis and Atlanta are entirely out of all reason;" and that "there is no reason why Atlanta, New Orleans, St. Louis, or Omaha should be made to pay a higher price for their pipe than other places near them" (page 103). No objection was made to this statement on the score of competency; nor can its competency be doubted (*Wiborg* v. *United States*, 163 U. S. at pages 657–658).

By unduly and vastly raising the normal price of cast iron pipe among communities which, by their geographical position, should have enjoyed special advantages, the combination has the indirect result of increasing competition in the northeastern or "free territory." This is shown by Thomasson's letter (pages 110–112), stating the policy of the Chattanooga company in view of the high bonusus paid by the Bessemer company for southern contracts. He figures out an advantage to the Chattanooga company in refraining from bids and taking its share of the bonus without contributing to the fund, and adds:

> If we cannot secure business in "pay territory" at paying prices, we think we will be able to dispose of our output in "free territory" and of course make some profit on that.

$13.00 to $14.75 per ton is stated in the same letter to be a profitable figure, and the Chattanooga company's propositions to northeastern cities after this letter (pages 104–107) show how the theory is carried into practice by giving those cities an advantage of several dollars per ton in price over the naturally better situated cities immediately adjacent to the works of these defendants. Mr. Llewellyn of Chattanooga, the chairman of the combination and one of its principal witnesses, was thus secretly inimical to its interests.

The letter announcing this scheme is dated January 2, 1896. We are furnished with the balance sheet showing payments and

divisions of bonus for the ensuing four and a half months (page 117). We find that Chattanooga during those months paid in $2016.25, and drew out $15,077.99 — truly a vindication of the wisdom, if not of the candidness, of this valuable witness.

Cast iron pipe, if we may believe Mr. Harrison of South Pittsburg, "has no market value" (page 214). "On account of the manner in which these contracts are let, the customer prevented the establishment of any market price" (page 216). We are therefore without any standard of reasonableness derivable from market quotations. The evidence, however, is overwhelming that in large portions of the country the price is half as much again what it ought to be.

There is, indeed, a large collection of affidavits stating that these prices are reasonable in the opinion of the affiants. Some of the affidavits are by interested parties, more or less discredited as above shown. Most of the rest are by persons who have no real expert knowledge. It will be remembered that cast iron pipe, on account of the peculiarities of its use, and on account of the high transportation rates, has no general market price throughout the country. Each local witness knows only that the combination gives him as low prices as any one else, knowing nothing of the conditions governing the price as it would be if the combination should dissolve.

Moreover the opinions are not accompanied by facts to back them, further than the single fact that the combination is able to underbid its competitors in certain localities. Such unsupported opinions have no weight under the rules governing expert evidence, as set forth in *The Conqueror*, 166 U. S. 110, 130–134, and cases cited.

Conclusion

Enough certainly has been said to show that this secret and hypocritical combination is in violation of the anti-trust law.

If necessary, it could easily be established that it is unlawful also at common law, so that the only question that the Attorney General would have had to consider, had the anti-trust law never been enacted, would have been whether the injury to the public

was sufficient to justify his filing a bill upon general principles of equity, as in the Debs case.

These water pipes and gas pipes belong to the class of articles, monopolies in which are especially disfavored by the law. (*Gamewell Fire Alarm Co.* v. *Crane*, 160 Mass., 50, 57.) Every combination tending to prevent competition for public contracts is absolutely void. (*Atcheson* v. *Mallon*, 43 N. Y., 147; *Whalen* v. *Brennan*, 34 Neb., 129, 153.) Combinations to divide up territory, and thereby maintain rates free from influence of competition, are void *per se* at common law, and their validity does not depend upon the result of any inquiry as to the percentage of profits actually obtained. (*Hooker* v. *Vandewater*, 4 Denio, 349; *Stanton* v. *Allen*, 5 Denio, 434; *Salt Co.* v. *Guthrie*, 35 Oh. St., 672; *Craft* v. *McConnoughy*, 79 Ill., 346; *Vulcan Powder Co.* v. *Hercules Powder Co.*, 96 Cal., 510; *Hoffman* v. *Waters*, 11 Weekly Law Bulletin, 358; *More* v. *Bennett*, 140 Ill., 69; *Bishop* v. *American Preservers' Co.*, 157 Ill., 284; *Nester* v. *Continental Brewing Co.*, 161 Pa. St., 473; *Oliver* v. *Gilmore*, 52 Fed. Rep., 562; *Anderson* v. *Jett*, 89 Ky., 375; *Urmston* v. *Whitlegge*, 63 L. T. N. S., 455; *Chapin* v. *Brown*, 83 Ia., 156; *Emery* v. *Ohio Candle Co.*, 47 Oh. St., 320; *Pacific Factor Co.* v. *Adler*, 90 Cal., 110; see also *Hilton* v. *Eckersley*, 6 E. and B., 47; *Ford* v. *Chicago Milk Shippers' Association*, 155 Ill., 166; *Railway Co.* v. *Railway Co.*, 61 Fed. Rep., 993; *Pittsburg Carbon Co.* v. *McMillan*, 119 N. Y., 46; *Santa Clara Co.* v. *Hayes*, 76 Cal., 387.)

Milwaukee Masons' and Builders' Asso. v. *Niezerowski*, 70 N. W. Rep., 166, was decided by the supreme court of Wisconsin on February 2, 1897. Sixty out of seventy or seventy-five mason contractors of Milwaukee made an association, paying into its treasury six per cent on all contracts taken by them, first submitting all bids for work to the association and raising the lowest bid six per cent before submitting it to the owner or architect. This was held an unlawful restraint of trade at common law, without the aid of any statute.

In the famous case of *People* v. *North River Sugar Refining Co.*, 54 Hun, 354, Judge Charles P. Daly, the distinguished counsel for the sugar trust, conceded "that combinations are

unlawful the design and effect of which necessarily is . . . to regulate and control the price of a commodity"; and Judge Barrett, referring to this concession, said that "all the cases, ancient and modern, agree that a combination, the tendency of which is to prevent competition and to control prices, is detrimental to the public, and consequently unlawful" (page 370, note).

It is therefore respectfully submitted that this judgment should be reversed, and a decree entered in favor of the plaintiff.

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V

COMBINATION IN THE STEEL INDUSTRY[1]

THIS case — a proceeding under the Sherman Anti-Trust Law — is largely one of business facts. The construction of that statute has been settled by the Supreme Court. *Standard Oil Co.* v. *United States*; *United States* v. *American Tobacco Co.* That construction has been applied in this circuit in the Keystone Watch Case[2] and the Powder Trust Case. It follows, therefore, that our duty is largely one of finding the facts and to those facts applying settled law.

The tests of the violation of this statute having then, as we have seen, been adjudged by the Supreme Court, namely, whether the acts in question "prejudice the public interests by unduly restricting competition or unduly obstructing the course of trade," it would appear the questions of fact for us to determine from the evidence are these:

First. Was the Steel Corporation, when this bill was filed in 1911, prejudicing the public interests by unduly restricting competition, or unduly obstructing the course of the steel and iron trade, between the states, or with foreign nations? If this question be answered "Yes," the law was then being violated, and an injunction should issue to restrain present and future violations.

Second. Did the Steel Corporation, when it was formed in 1901, either by the intent of those forming it, or by the inherent nature of that company's contemplated acts, prejudice the public interests by unduly restricting competition or unduly obstructing the course of the steel and iron trade, interstate or foreign?

[1] *U. S.* v. *U. S. Steel Corporation,* U. S. Dist. Court, N. J. decided June 3, 1915; 223 Federal Reporter, 55. Elaborate details are also given in the U. S. Bureau of Corporations, Report on the Steel Industry, July 1, 1911. Stevens, *op. cit.,* chapter VI, reprints testimony of Gates, Gary, Schwab, and Carnegie before the Stanley Committee.

[2] These cases are reported in Chapter XVII, *infra.*

If this question be answered "Yes," then the law was violated, and the Steel Corporation must be adjudged originally illegal. If illegal, it must be dissolved, because only thus can its inherent nature be prevented from continuing to work further violations of the statute. On the other hand, if these questions are negatived, then the Steel Corporation should not be dissolved, but permitted to pursue that usual course of trade, which it was the purpose, as we have seen, of this statute to protect. It will thus be seen that, as stated at the outset, this case is practically one of business facts.

Turning, then, to the first question, let us address ourselves, first, to the iron and steel trade here in the United States, and inquire whether the evidence satisfies us that the Steel Corporation, when this bill was filed in 1911, was then prejudicing the public interests by unduly restricting or unduly obstructing the steel and iron business of the United States. In considering that question, a number of fields of inquiry naturally suggest themselves. Had this company in 1911 a monopoly of the steel and iron trade of the country? What had been and was then its business conduct towards its competitors? Was it fair or unfair? Had it forced or was it forcing others out of the steel trade by unfair conduct? Had it prevented others from entering it? Was it then exacting or had it exacted from the public undue prices for its products? Had it lowered the character of its product? Had it cut down or was it cutting down, its output so as to restrict proper supply? Had it taken advantage of its power to unduly reduce wages? All these, as we have seen from the Standard Oil, the Tobacco, the Powder, and Keystone Watch cases, were inquiries by which the question could be determined whether the Steel Corporation was acting, as the Supreme Court said in the Standard Oil case, with "the legitimate purpose of reasonably forwarding personal interest and developing trade," or, on the other hand, "with the intent to do wrong to the general public and to limit the right of individuals."

Now as trade is a contest for it between different persons, and the gain of that trade by one means the loss of it to another, it follows that the person who best knows whether the man who

gained it, gained it fairly, is the man who lost it. If there is monopoly, if unfair business methods exist, if the course of trade and fair trading is throttled, we can find proof of it from business competitors. Trade competitors are the first to feel the pinch of unequal, unfair, and undue restraint of the natural and normal course of trade. Being the first to suffer, they are the keenest to condemn. Turning, then, to this Steel Corporation's competitors, let us decide from the proofs whether the Steel Corporation had, when this bill was filed, a monopoly of the iron and steel business of the United States.

We turn, first, to finished rolled products, because they are the basic supply to the vast number of varied industries throughout the country dependent thereon. If all these minor industries are dependent on a monopolized source of an indispensable base, we can say, without going further, that not only such industries, but the general public, are prejudiced; for, as said and held by the Supreme Court in the Tobacco case, wrongful purpose and illegal combination are established "by the gradual absorption of control over all the elements essential to the successful manufacture of tobacco (steel) products."

What, then, are the facts in reference to finished rolled products? In that regard, the evidence is that in 1911 the finished rolled product — which excludes pig iron, steel castings, and ingots — of the United States (using in this opinion, when quoting figures, round numbers, and by the term "Steel Company," or "Steel Corporation," meaning the United States Steel Corporation) was 19,000,000 tons. Of this tonnage the competitors of the Steel Corporation produced 54 per cent, or 10,300,000 tons, while the Steel Corporation made 8,700,000 tons; but not only did its competitors produce in 1911 the major part of the country's finished rolled product, as above, but judging from the past, the present proportionate lead of the competitors bids fair to increase. In 1901, when the Steel Company was formed, the total finished roll product of the United States was 13,000,000 tons. This was substantially divided between 49.9 per cent made by its competitors, and 50.1 per cent by the Steel Company. While both together have since increased the nation's product from 13,000,000 to 19,000,000 tons, yet of this 6,000,000

increase its competitors produced 3,400,000 tons to the Steel Company's 2,600,000 tons.

Taking steel ingots, another basic supply on which great numbers of finishing industries are ultimately dependent, we find that while in 1901, of the 13,000,000 tons of the total American ingot production, the competitors of the Steel Company only made 4,500,000 tons, as against the Steel Company's 8,500,000, yet by 1911, in the country's vast increase from 13,000,000 to 24,000,000 tons, the competitors had increased their production by 6,500,000 tons, while the Steel Company had only increased 4,500,000. In other words, while the Steel Company produced in 1901, 66 per cent of the country's ingot production, it was producing but 54 per cent in 1911.

In pig iron, the basic supply of foundries, finishing mills, and other dependent industries, the relations were slightly the other way. In 1911, out of a total cast of 22,000,000 tons of pig iron, only 12,000,000, or 54.8 per cent, were made by competitors of the Steel Company, as against 9,000,000, or 56.8 per cent, made by such competitors in 1901, out of a total of 16,000,000—a decrease of 2 per cent.

These facts and figures bearing on basic supplies of the country's dependent iron and steel industries satisfy us that there is no monopolistic control anywhere of such basic factors as ingots, pig iron, and finished rolled products, and the testimony hereafter referred to satisfies us that any substantial producer of such basic articles can, by selling such products at such lower price as he sees fit, compel all producers of such supplies, including the Steel Corporation, to also lower their prices. So, also, monopolistic control of finished steel articles in wide use would be a matter of grave public prejudice. Taking for example, wire production, in which, through fencing, nails, and the great range of articles made from wire products, so many people are interested. When the Steel Corporation was formed in 1901, of the 9,000,000 kegs of wire nails then made in the United States, the competitors of the Steel Corporation made 3,000,000 kegs, and the Steel Corporation 6,000,000. By 1011, the country's production had grown to 13,000,000, but of the 3,500,000 of increase the Steel Corporation made 1,000,000 as

against its competitors making 2,500,000. The net result was that, when this bill was filed, the Steel Corporation's competitors had 6,500,000 and the Steel Corporation 7,000,000 of the country's total production of 13,500,000 kegs. So of wire netting, fencing, and other wire products in general use. The general average of the nation's total production made by competitors when this bill was filed was 78 per cent. It will be seen that in this particular respect, due, no doubt, as we shall see, to the growth of its foreign trade in wire products, the Steel Corporation had slightly increased its proportion from 20 per cent of the total product in 1901 to 22 per cent in 1911. But at the same time it will be noted that, as the very large part of the Steel Corporation's increase in wire products was made in foreign trade — the proofs (volume 10, p. 3902) show that only 42 per cent of the Steel Corporation's wire product of 1911 was sold in the United States — it was in 1911 making relatively much less of the wire products consumed in the United States than it was in 1901.

In the important item of structural steel, used in bridges, steel framed buildings, steel car frames, etc., the steel corporation's competitors produced about 67 per cent, and the Steel Corporation 33 per cent. And for the same reason as shown above, in the growth of the foreign trade, it will be seen by an analysis of Defendant's Exhibit (Vol. 3, p. 317, and Vol. 2, p. 204) that in structural shapes, as in wire products, the Steel Company was in 1911 making relatively less structural articles of this country's consumption than it was in 1901.

So, also, in steel rails. In 1901, the competitors of the Steel Company made 1,100,000 tons of steel rails, and the Steel Company 1,700,000. In 1911, its competitors made 1,200,000 tons, an increase of 100,000 tons, while the Steel Company made 1,600,000 tons, a decrease of 100,000 tons.

Summarizing our study of the proofs of this general subject, of the relative part of the Steel Company and its competitors in the total iron and steel production of the country, and their relative part in the home market, we find that, taking the ten years from 1901, when the Steel Company was formed, until 1911, when the Attorney-General filed this bill to dissolve it, its com-

petitors, starting in 1901, with making 49.9 per cent of the nation's production of finished rolled product, including structural materials, rails, sheets, rods, and bars, had by 1911 so increased their relative proportion that they were then producing 54.3 per cent of the nation's iron and steel output. And confining ourselves for the present to the production of 1911, used in the trade of the United States, which alone we are now considering, we find that, of the total amount of such iron and steel products in the whole market in that year, nearly 60 per cent was produced by the competitors of the Steel Company. These conclusions, based as they are on proven, practical business facts and figures, show a strong trend away from any monopolistic absorption or trade-restraining control of iron and steel manufacture or markets of the United States by the Steel Corporation. On the contrary, these figures show a strong trend in that manufacture and market toward an even greater absorption thereof by the virile and growing competitors of the Steel Company. And this leads us, in an adequate discussion of the case, to at this point take up the character of the competition in the steel and iron business in this country; for we may rest assured of the practical fact that where in any business there exists a healthy, normal, unrestrained, and virile competition, which all are free to enter, the individual has full freedom of business opportunity and the public is in no danger of prejudice from monopoly or trade restraint.

When the steel business of the United States is referred to, one thinks of it as practically being in the hands of the United States Steel Corporation. Circumstances have made this natural. The manufacture of iron and steel in their basic form is confined to local districts. Outside of these localities and outside of those engaged in the steel business, there was, prior to 1901, but little general knowledge or appreciation of its magnitude and its basic relation to the general business of the country. When, therefore, this great steel company was quickly formed in that year and became at once the largest corporate capitalization known, it naturally and at once became associated in the general mind with absolute monopolistic control. But the fact that the Steel Corporation after due selection by it of such lines

of finishing mills as were deemed necessary to carry out its plans left outside of it a most strenuous body of strong competitors was not then generally recognized. The names, location, and resources of those competitors were not then, and indeed are not now, known to those outside the steel and iron business. Nor was the significance of the anti-monopoly competitive powers and policies of such competitors appreciated. Indeed, the business fact above found, namely, that in 1911, when this bill was filed, the competitors of the Steel Company were making and marketing nearly 60 per cent of the steel and iron produced in the United States, would surprise many. Since therefore the gist of monopoly is the suppression of competition, we deem it pertinent to ascertain from the proofs the character and steady increase of competition in the iron and steel business since the Steel Corporation was formed. In doing this, we here note of its great competitors such only as have, in the ten years of competition between them and the Steel Corporation, made a higher proportionate gain of business than the Steel Corporation itself.

Taking the Steel Corporation as the basis of comparison, we may say that while the proofs show a very material increase of 40-odd per cent in the Steel Corporation's business from 1901 to 1911, yet this very substantial increased percentage of the Steel Corporation's own business was less than that made by each of its great competitors as follows:

Company	Location	Increase of Production from	Percentage of Increase
Bethlehem Steel Co.	So. Bethlehem, Pa.	1901 to 1913	3779.7
Inland Steel Co.	Indiana Harbor, Ind.	1901 to 1913	1495.9
La Belle	Wheeling, W. Va.	1901 to 1913	463.4
Jones & Laughlin	Pittsburgh, Pa.	1901 to 1912	206.7
Cambria Steel	Johnstown, Pa.	1901 to 1913	155.5
Colorado Co.	Pueblo, Colo.	1901 to 1912	152.8
Republic Iron & Steel Co.	Youngstown, Ohio	1901 to 1912	90.8
Lackawanna Steel Co.	Buffalo, N.Y.	1901 to 1911	63.2

Taking up these companies one by one, it will be seen that in location, facilities, capital, and basic supplies, they show such strong past, present, and prospective competition as affords just ground for concluding that the steel and iron business of this country is not being, and indeed cannot be, monopolized by the

Steel Corporation. For the real test of monopoly is not the size of that which is acquired, but the trade power of that which is not acquired.

Turning, first, to the Atlantic seaboard, we find there is a competitive group composed of the Bethlehem Steel Company, the Pennsylvania Steel Company and its subsidiary, the Maryland Steel Company. The two latter companies are additional to the above list, and are here referred to only to note their tidewater location as an advantage which the Steel Corporation with its inwardly located works does not possess. The works of the Pennsylvania Steel Company are near Harrisburg, Pa., and those of the Maryland Steel Company at Sparrows Point near Baltimore. These two companies have a combined capital and surplus of some $66,000,000 and with large extensions in view. Their ore supplies are drawn from the great Cornwall ore beds of Eastern Pennsylvania, and from Cuba, where they have inexhaustible supplies of Bessemer ore, which can be worked by steam shovels and are close to tidewater. Three matters have impressed us in reference to this seaboard competition: First, that the eastern seaboard iron and steel competition of the Steel Corporation has an ore supply wholly independent of Lake Superior; second, that their location near the seaboard gives in many cases substantial freight advantage over the Steel Corporation; and, thirdly, that the greatest advance in ore and steel production in the past ten years has been made by a seaboard competitor of the Steel Corporation, the Bethlehem Steel Company. And as bearing on the question of the alleged object of those who originally formed the Steel Corporation to monopolize and unduly restrain competition and obstruct trade, it is to be noted that the striking growth and development of the Bethlehem company was undertaken by one who helped form the Steel Corporation, who served as its first president, and who, if the object for which the Steel Corporation was formed was to monopolize the iron and steel business or to restrain trade, was warned of that intent. That such a man should attempt to build up a competitive business and succeed in expanding it as has been done shows that he at least was convinced that the field of fair, free, and full competition was open to him and others who

desired to enter the steel business, and that the Steel Corporation had neither the business purpose nor the business power to monopolize the steel business or to throttle the growth of competition.

As we shall see later, the market reach of basic iron and steel plants is measurably restricted to its own district by freight limitations. The supplies from which steel is made and the basic articles into which it is turned are of such bulk and weight as to thus localize or restrict their markets. Freight forbids such heavy product being hauled to far-removed markets. The existence and maintenance of strong competitive steel production on the seaboard is therefore a matter of grave import to the great section of the United States immediately tributary to the Atlantic Coast. Into this seaboard region the Steel Corporation enters under freight burden, its bulk mills being substantially in the Chicago and Pittsburgh districts. The proofs show that its seaboard competitors named have, as noted, abundant ore supplies, cheap water freights, and a great accessible surrounding market. Without entering into detail, we refer to some suggestive facts in the proofs. For example, the proofs show that the Maryland Steel Company, through its coast line water freight of $2.50 per ton, so covers the territory supplied by Mobile, Galveston, and other Gulf of Mexico distributing points as to exclude from that territory even the product of the Tennessee Coal & Iron Company, now owned by the Steel Corporation, which pays a railroad freight of $3.40 per ton. The proofs further show that, with the enlargement of the Erie Canal system, Lake Superior ore will be canal freighted from Buffalo to New York harbor at 28 cents a ton less than the same ore is rail freighted from Lake Erie ports to the Pittsburgh district. With the enlargement of that canal, the proofs are that blast furnaces are now planned for location on seaboard waters in New York harbor limits. And it should be here noted that the proof is that the whole steel industry of the United States could be duplicated on the Atlantic seaboard and inland as far as Pittsburgh, and could be run on ores brought from Chili and Brazil alone. Lake Superior ores of the same metallic unit grade as the Brazilian would, in the view of the Michigan Tax

Commission, cost $7 a ton delivered at the Atlantic seaboard, as against ore of $3 from Brazil, which the report states has "a tremendous field of high grade Bessemer iron ores running 65 to 68 per cent metallic iron." As to the Cuban ore, the proof is:

The total cost will not in any case exceed $2.25 per ton, and in ordinary shipping seasons will probably not exceed $2.10 per ton. This means that the ore reaches Philadelphia at a net cost of 4 cents per unit of iron. It is the cheapest ore supply in the world delivered at eastern Atlantic ports or in German or English ports. . . . In normal years, Lake Superior ores at the extreme eastern point at which they could possibly be shipped to meet eastern or foreign ores would have to get a price of 9 cents a unit in order to compete.

These facts and figures show that there is no basis on which to attempt ore monopoly. The proofs further show that, to adequately enter this seaboard territory and meet the competition of those located on the seaboard, the Steel Corporation was forced to establish large local distributing warehouses on the seaboard. For example, the corporation had established, amongst several others, warehouses on the Atlantic Coast near New York carrying $2,000,000, and one at San Francisco carrying $4,000,000 of diversified steel products.

Proof of the strength and growth of this seaboard competition is found in the record of the Bethlehem Steel Company. That company in 1901, its first year of competition with the Steel Corporation, made 18,000 tons of finished steel product, which was largely confined to rails. By 1913, it had increased its product to 700,000 tons. During that time it had also entered into competition in structural steel, armor plate, and varied steel products. Indeed, its chief products, structural steel, and open-hearth rails, of which it is making 200,000 tons, have been developed since 1908. From 4,000 employees it has grown to 15,000; it has in view further integration to the extent of making all the finished products made by the Steel Corporation. Its ore supply of a million and a half tons a year comes from Sweden, from the Adirondack regions in New York, from Chili, and from Cuba, where it has practi-

cally inexhaustible reserves. The proofs as to these Chilean ore fields show that this corporation and other tidewater steel plants are wholly independent of Lake Superior reserves. The Chilean beds outcrop; they are stripped instead of mined; they are within a short distance of the coast to which they are gravity dropped. They are magnetic, hematite, and dry — a great saving in transportation, as will be appreciated by those familiar with the wetness of Lake Superior ores which necessitate the carrying of thousands of tons of water. The proofs show the substantial character of this competitor with a surplus and capital of $55,000,000 and further integration in view.

Referring at this point to the existence of a fair and open competitive field, as sensed by practical men in the iron and steel industry, we gain light from the proofs in reference to the Youngstown Sheet & Tube Company of Youngstown, Ohio. That company does not appear in the foregoing list because it came into existence after the Steel Corporation was formed. It is an inland company. Its ore supply is from Lake Superior. It started the year after the Steel Corporation was formed. It purchased its reserve ore supply in 1903. It began with an investment of $600,000, which in the succeeding years has been increased to over $29,000,000. By 1913, it had an annual capacity of 1,000,000 tons of ingots and sold that year over 800,000 tons. This company is cited as evidencing three things: First, that the men in the steel and iron trade immediately after the Steel Corporation was formed felt they had an opportunity to enter and prosper in the steel and iron business, both in the home and foreign markets; second, they felt secure about their basic ore supply; and, third, they were free to and did build up a great business in making steel ingots, one of the primary products or bases.

Coming next to the Pittsburgh district, we find a strong competitor of the Steel Corporation in the Jones & Laughlin Company, which, at the time of the Steel Company's formation, the proofs show was then so integrated as to make "a greater variety of product than any other steel or iron company in the country." In 1901, its finished product alone was nearly one half million tons. By 1912, it had increased that production to

one and a half million tons. During that time it had integrated still further by building large additional works and had entered into competition with the Steel Company and others in the manufacture of tin plate and wire rods. Like all these other competitors mentioned, the Jones & Laughlin Company is thoroughly "integrated"; that is, it has its own basic supplies and carries on its work in continuous process from ore to diversified finished steel products. It has large reserve holdings of ore in the Lake Superior region and an ore fleet on the Great Lakes with a carrying capacity of 40,000 tons. It has over $50,000,000 capital and a large surplus.

The history of the next company is illustrative of the feeling of confidence and security among practical steel men, which warranted them in making since the Steel Corporation was formed large expenditures and entering into competition in the steel business. The Republic Iron & Steel Company of Youngstown, Ohio, was, in 1901, engaged principally in making iron. Its finished product that year was some 500,000 tons. It has since expended $25,000,000 in changing its business from iron to an exclusively steel one. Like all other steel makers, the Republic company's policy has been one of simply following the progressive and universal practice of integration incident to the development of the use of steel. The Republic company's process of integration its president well describes:

> We have practically eliminated all our scattered iron mills, have concentrated them in the operation at a few points of production. So, to-day we produce practically but little iron and are manufacturing about 1,000,000 tons of steel per annum. This is what we call an integrating process; that was part of it, the addition of the mineral and coke and blast furnaces, and balancing up operations generally, completing the integrating process. . . . This integrating process that I speak of attended our development of the steel end of our business. We did not need it so much when we were simply manufacturing iron. It was done for economic and trade reasons, on account of the increased demand for steel and the decreased demand for iron.

The Republic has increased the range of its product and production until it is now a million and a quarter tons and ex-

tends all over the United States and Canada. It has gone into the Birmingham, Ala., field, where it has plants, as well as in Pennsylvania, Missouri, Illinois, Indiana, Iowa, and Michigan. It has acquired 40,000,000 tons of Lake Superior ore reserve and 80,000,000 in the Birmingham district, and has a lake fleet of 18,000 tons. Its growth during this time was such that it is producing one twenty-fifth of all the steel produced in the United States and one thirtieth of all the iron. From a study of the testimony there is no doubt that the men who made these large expenditures in 1906 were satisfied that the field of fair business competition in the iron and steel business was open to them. These expenditures were made in completely integrating its manufacturing facilities. This integration consisted in increasing its blast and open hearth furnaces and ore supply and carrying their basic product forward to completion by additional plants which included finishing mills for merchant bar, for sheet bar, for billets, and for plate in addition to galvanizing works, rivet, spike, bolt, and nut departments, and by-product coke works. They have no more to fear from the competition of the Steel Corporation than they have from that of any other of their other competitors. The testimony of this company's president, who like the Cambria's president, was called as a witness both by the government and the Steel Company, is instructive, on that point. It is:

Q. Where is the market for your product?

A. All over the United States and Canada.

Q. Has the Steel Corporation in your opinion power to put the Republic out of business?

A. I think not.

Q. Has it the power to put its competitors generally, or any of its principal competitors, out of business?

A. I would say not.

Q. What is your reason for thinking that they have not that power?

A. I would have two reasons: One, that they have not the physical ability to do it; and, secondly, if they attempted it, they would involve their own market to such an extent that they would suffer equally with us. What I mean by physical is this: Their principal competition, companies like ourselves and others as strong as we are, are properly integrated; in other words, being self-contained on raw

material, well equipped, and at least fairly well managed and properly financed, so that a combination of that kind would give us as much power to produce within somewhere a close approximation of their cost; at least their difference would not be so great that they could put us out of business. They have some advantages, and so have we.

Q. Now, as to your second reason, that it would involve them in loss as well as you, what do you mean by that?

A. Well, to illustrate, we might have a customer, we will say, in Michigan, engaged in the manufacture of agricultural implements, and another one in Illinois or Indiana. If we should sell in Michigan steel bars and plates that enter into the cost of production of a machine at a less price to A in Michigan, than we do to B in Illinois, we would probably soon hear from B in Illinois, because those two men would naturally compete in the general market of the United States with their machinery. So it would be with all other fabricated products made from steel, the markets are interrelated and interlaced to such an extent that you cannot reduce prices, in my judgment, in one market, without affecting in a short time the market elsewhere for the same commodity.

Q. Could the Steel Corporation localize a destructive warfare against its competitors?

A. Not in my opinion.

Q. Why not, if there is any other reason than you have already indicated?

A. I should say that the reason I have already indicated would be a complete answer to that thought. There is a sympathetic relationship existing between all markets that is so close that my experience would compel me to say that you could not affect the price in Chicago without affecting the price in New York. As a matter of fact, that is the experience that we have had.

Q. And could the Steel Corporation wage a destructive warfare against any one of its competitors without involving all of them?

A. No; I would say not.

We have referred above to competitive steel conditions on the Atlantic seaboard as shown by the proofs. Those proofs also show how competition to the Cambria, Jones & Laughlin and the Steel Corporation has grown on the Pacific Coast. This competition has increased since the Steel Corporation was formed. Mr. Pigott testifies his company has built at San Francisco open hearth furnaces with a capacity of 30,000 tons;

bar mills, with 30,000 tons capacity; and at Seattle a rail re-rolling mill with a capacity of 30,000 tons. For its basic supply this company is wholly independent of the Steel Company, Jones & Laughlin, the Cambria Steel and all eastern companies doing business on the Pacific Coast. This is clearly shown by the proofs. This company gets one half of its pig iron from China and the balance from the Republic company and the Tennessee Coal & Iron Company. The proof is that the freight paid to deliver the Tennessee company pig iron from Birmingham, Ala., to San Francisco is $10.08 per ton. The proofs further show that the Chinese pig iron is delivered at Pacific points at a freight rate of $3.70 per ton. If to this $3.70 be added the price of the pig iron, $6.20 per ton, it will be seen that the Chinese pig iron at $6.20, plus freight $3.70, $9.90, can be paid for and delivered on the Pacific Coast for about the amount, $10.08, the Republic and the Tennessee Company pay for freight alone. As the proofs further show that pig iron from India is being delivered in San Francisco from Calcutta at an expense of $12.38 per ton, namely, price of pig iron $5.40 plus freight $6.98, it will be seen that the future basic supply of this and other companies that may spring up on the Pacific Coast can be had of Asiatic pig metal wholly independent of the Steel Corporation and other eastern competitors. In view of the further proof that the ores on the western coast of Mexico, and necessarily those of Chili, are also available, and that the improved practice in steel making makes ores now usable which were formerly not so, the conclusion is warranted that the field for all possible development on the Pacific Coast in the steel business is wholly free from any monopolistic control whatever. It will thus be seen that a substantial steel industry in rails, bars, and open hearth steel has in fact grown up on the Pacific Coast, while in competition with the Steel Company, a competition which Mr. Pigott describes, "from the standpoint both of a customer and a competitor," "has been beneficial."

Later, we shall note the testimony of competitors as to their relation to the Steel Corporation, but before referring to individual relations, we deem it proper to here refer to some general

phases of monopoly which affect all competitors. One of these was the practice by large companies of exacting freight rebates from railroads under threat of diverting shipments elsewhere. These practices were common up to the time of the ending of the old era of freights unregulated by the government.

On January 28, 1905, Congress directed the Secretary of Commerce and Labor to investigate the steel and iron industry of the country with a view to ascertaining to what extent the United States Steel Corporation controlled the output and prices of finished product made by independent companies dependent upon it for their raw material and to report any restraints by it of commerce, foreign or domestic. James R. Garfield, who as Secretary of Commerce and Labor, made this examination, was called as a witness. He testifies he had made an investigation and examination of the railways in a similar manner to that made in the Standard Oil, and found no rebating whatever by the railroads to the Steel Corporation. That he was justified in his conclusion is strengthened by the fact that at a meeting of the Steel Corporation's executive committee in 1901, called to consider the policy of the company towards railroads, the minutes show the position taken the first year of the corporation's formation by its chairman and there recorded, was "that we cannot afford to take the position of asking any railroad, directly or indirectly, to discriminate in our favor." This policy was later emphasized in a letter sent to the presidents of the railroads handling the Steel Corporation's freight, as follows:

Personal Sept. 20, 1905

DEAR SIR: As you know, this corporation long since adopted the unalterable policy of recommending to subsidiary companies in which it is interested, that under no circumstances should rebates be solicited or received contrary to law. This policy will be strictly adhered to and it is hoped and expected your subordinates will be advised and instructed accordingly. If any one should at any time violate his instructions in this respect, notice of the same should be promptly given to the president of the subsidiary company interested and also to the undersigned.

Yours very truly,

W. E. COREY, *President*

In view of this announced policy of the corporation of the investigation made by the Department of Commerce and Labor, of the absence of any complaints by any competitor, and of no proof of any freight rebate being given, we are justified in concluding that the Steel Corporation has not used, or sought to use, freight rebates as a means of undermining its competitors, or of monopolizing business.

We next turn to ruinous trade wars against competitors which, as we have seen, was one of the features of attempted monopoly denounced by the Supreme Court. In that connection it is to be noted that under conditions incident to the steel trade the power of a large steel company to carry on a ruinous trade war against any particular competitor does not exist in the iron and steel industry. The customers of the great steel companies are large jobbers and the purchasing agents of other companies, who are in the closest touch with every fluctuation of the steel market. The result is that any effort on the part of any one of these great steel companies to inaugurate a trade war by ruinously underselling a competitor would at once, owing to the sensitiveness and interrelated character of the steel market, result in forcing the company that was thus ruinously selling in any particular market or locality to in the same way ruinously lower its prices in every other community. In that respect, the president of the Youngstown Sheet & Tube Company, a competitor, testified that, if the Steel Corporation attempted such a course, "they would involve their own market to such an extent that they would suffer equally with us." The testimony of the president of the Cambria Steel Company, already quoted, is to the same effect, as well as that of the president of the Republic Iron and Steel Company. And the practical impossibility of such a course is shown by Judge Gary, where he testifies:

> I feel certain that by reason of our integrated proposition we had the advantage in cost of production over our competitors generally. If any one having advantage in any business is willing to sell down to his cost price, of course he would live while his competitors would starve; but that is a most unnatural position for any producer to take and long continue.

In view, therefore, of the uncontradicted proof of those familiar with the steel business that no such ruinous trade war could with profit to itself be carried on by the Steel Company against a competitor, and in the absence of proof of any effort by it to harass them by such conduct, we are warranted in concluding there has been no attempt by the Steel Corporation to monopolize or restrain trade through ruinous trade wars against its competitors. For of the conduct of the Steel Corporation, the views of its competitors is the best gauge. Monopoly and unreasonable restraint of trade are, after all, not questions of law, but questions of hard-headed business rivalry, and whether there is monopoly of an industry, whether trade is subjected to unreasonable restraint, whether there is unfair competition, are facts about which business competitors best know and are best qualified to speak. And it may be accepted as a fact that where no competitor complains, and much more so, where they unite in testifying that the business conduct of the Steel Corporation has been fair, we can rest assured there has been neither monopoly nor restraint. Indeed, the significant fact should be noted that no such testimony of acts of oppression is found in this record as was given by the competitors of the Tobacco or Standard companies in the suits against those companies. We have carefully examined all the evidence given by competitors of the Steel Corporation. We have read the testimony of customers who purchased both from it and from its competitors. Its length precludes its recital here, but we may say its volume, the wide range of location from which such witnesses came, and their evidently substantial character in their several communities make an inevitable conclusion that the field of business enterprise in the steel business is as open to, and is being as fully filled by the competitors of the Steel Corporation as it is by that company.

We have noted above the remarkable growth of the Youngstown Sheet & Tube Company, which came into existence in 1905, and in the meantime has grown to be a very important competitor of the Steel Company. The testimony of James A. Campbell, its present president, who was called as a witness by the government, so fully covers the subject of the attitude

of the corporation toward its competitors and the purchasing public that we quote it at length :

A. My experience is that it is the best competition we have ; that they are open and above board in all of their dealings. Their prices are either published, or we get direct information from them or through our customers as to what their price is, and we find that their price is practically the same to everybody. With other competition that we have, with the independents, for instance, the independents vary more in their prices, and we never quite know what their price is. It may be one thing to-day and another to-morrow, and they do not conduct their business in the same way, because it is a smaller business and more of an individual business ; and they will make prices according to the class of material pretty largely and the class of orders. So we were not as capable of gauging how they are conducting their business as we are in regard to the subsidiary companies of the Steel Corporation.

Q. Is your competition with these subsidiary companies of the United States Steel Corporation active and energetic and vigorous competition ?

A. It is — very, at times. We sell to many of the same people that they do, the same class of material.

Q. Have you ever known of their having made low prices in a limited section of the country for the sake of attempting to put a competitor out of business ?

A. I think not. I do not recall any time, with any company.

Q. Have they, in your experience, been guilty of any unfair methods to suppress competition ?

A. I think in the early days — I did think in the first two or three years we were in business that there were some things done, and I think done without the knowledge of the higher officials, that were unfair; but those disappeared promptly, and there has been nothing of that kind, nothing but the fairest competition in every respect for the last seven or eight years.

Q. When the market has been falling, what has been your experience as to the prices which they have maintained as compared with those of the independents ?

A. In depressed times, when there is not nearly enough business to keep all of the mills operating to their full capacity, their prices are usually higher than the independents. In good times, when the mills are all working to capacity, their prices are usually lower than the independents. The independents will accept bonuses and do things

of that kind that I do not think the corporation will do. So that I think the general effect is for the steadying of prices and making them better for the country at large, and of course in dull times, it is a great protection to the smaller manufacturers to have them keep their prices up, when business is slack, than it would be if they went out like the Carnegie Steel Company did in the early days and took all the business and shut the other people down.

We next turn to that most injurious feature of monopoly's wrong to the public, to wit, increase in the price of its product or a deterioration in quality. Turning, first, to the basic question of quality, no dispute arises under the proofs. They are simply uniform that both with independents and the Steel Corporation, there has been a steady bettering of quality in steel products. This factor of improving its product has been recognized by the Steel Corporation, and a study of the testimony of its buyers satisfies us that this progressive growth in quality by the Steel Corporation has been the principal means by which it has acquired and held its business.

Turning next to the increase in price, we are met by two aspects of the case. Two learned experts have been called, one by the government, and one by the Steel Corporation, who draw different conclusions as to whether there was an increase or decrease in the price of iron and steel products. The deductions of both are supported by weighty contentions and numerous enlightening charts. The able reasoning of both has had the thoughtful consideration the standing of the two men challenges. We may note that the different ranges of time they had taken, as the basis of their reasoning, really makes them reason about two different things, but apart from that, we think whatever may have been the range of iron and steel prices during the periods of consideration selected by each, the proof is that in these days of quick communication the general price of steel and iron products cannot be localized, but is interdependent in this country and, indeed, internationally so. That proof is that when there is an oversupply, even in the European steel and iron market, that market tends to unload on the American steel market, and on the other hand, when there is an oversupply here, this country seeks to dump on their markets at any price.

It will also be observed that so sensitive and interrelated is the price of steel and iron that a drop in price of any particular branch of steel leads to a drop in all other branches.

No evidence is produced showing that there has been at any time an arbitrary or unreasonable increase in price of any of the numerous products of the Steel Corporation. On the contrary, the proofs show decreases in important steel products, among which we may refer to wire nails which from selling in 1901 at $51, when the Steel Corporation was formed, were, in 1911, when this petition was filed, selling at $36. During the same time, steel bars receded in price from $33 to $25. Steel beams dropped from $36 to $27; billets from $27 to $24; and a statement taken from the Steel Corporation's accounts shows there was between 1904 — a date when the Steel Corporation may be said to have been fairly systematized and under way — and 1912, a decrease in fabricated prices received by the company of 19 per cent, and of all other products, of 11 per cent. Summing up the business result, the president of the corporation testified the Steel Corporation was in 1912 getting about $8 a ton less for materials in the domestic market than they were receiving in 1904. Moreover, it should not be overlooked that during these years there were substantial factors of increased expense in the cost of manufacture. The freight on coke, of which the corporation uses some forty thousand tons a day, has increased 12 per cent since 1901; the freight on limestone, which constitutes one third of a furnace's burden, has increased 10 per cent since 1901; and iron and steel wages have increased 28½ per cent.

Standing aside for later discussion the matter of the Gary dinners and the meetings following them, through which it is alleged the Steel Corporation in coöperation with its competitors unduly restrained and obstructed the normal course of the steel trade, and confining ourselves to the fixation or control of prices by the Steel Corporation itself, or its subsidiaries, we may say we have found in this record no proof by any witness showing any instance in which the Steel Corporation or its subsidiary companies has set either an arbitrary, exorbitant, unfair, or controlling price on any one of its numerous products. It is

a mere truism to say that the fixing and maintaining by a manufacturer of a fair price above cost is not only a right but a commercial necessity, and any other course must end in his bankruptcy. When such fair prices are departed from and they are unreasonably raised and exacted from the purchasing public, the public is prejudiced thereby. On the other hand, when that price is so unreasonably lowered as to drive others out of business, with a view of stifling competition, not only is that wronged competitor individually injured, but the public is prejudiced by the stifling of competition. Between these two price extremes, there must, in the nature of things, be a considerable zone of reasonable price variation, and what is a fair price is a question which can only be determined by a careful ascertainment from cost sheets and other data of such fair price. In the present case neither side has furnished this court with proof from which we could intelligently determine whether the prices charged by the Steel Corporation for any of the numerous articles here involved, beginning for example with pig iron and ending with rails, were unfair, exorbitant, or unreasonable. In the absence of such testimony, it is manifest that for this court to assume that the prices at which any of these articles were sold by the Steel Corporation and its competitors were unfair would be to base such conclusion on surmise instead of proof. But there is not only this absence of testimony in regard to the prices received being unfair and exorbitant, but there is, on the other hand, affirmative testimony, which we cannot disregard, and which, as it seems to us, constrains us to conclude that the prices of the product sold by the Steel Corporation have been the result of the joint action of the law of supply and demand and of that vigorous rivalry which has at all times existed between the Steel Corporation and its competitors. In that respect we have the testimony of the Steel Corporation's great competitors, of large and small manufacturers, over the whole country who purchased basic steel products and put them through other stages in their mills and factories; of jobbers and warehousemen who buy and hold for sale large stocks of steel products. The testimony of these men — and there is no testimony to the contrary — is that the

iron and steel trade in the various products of the Steel Corporation is and has been open, competitive, and uncontrolled, and that all engaged therein have free will control in selling at their own prices. This important fact we shall not leave to here stand as a statement of a conclusion reached by us from a study of the testimony; but, at the risk of unduly prolonging this opinion, we shall here spread on record the testimony of a few witnesses on that subject so that he who runs may read.

In taking up that question, we have, in the first place, the proof that so far as the prices charged by the Steel Company are concerned its practice has uniformly been to give the utmost publicity to such prices. In that regard, Charles H. Schwab, a former president, testified as already noted above:

> In the beginning of the Steel Corporation, during my presidency, the policy of the corporation (was) . . . of naming a price for our product not only to our customers, but openly through the trade journals, if you will, because I used to give it to the *Iron Age* and the *Iron Trade Review* each week, and the sticking to these prices throughout the trade; there probably were exceptions of a minor character to very large consumers, but as a rule, during my presidency of the corporation, the prices of its product were fixed and published and they were what were charged the customers. . . . So far as I know, from the point of view of a competitor (the witness is now president of the Bethlehem Steel Company) they have adopted since that time practically the same policy.

The testimony of the sales manager of the La Belle Iron Works of Wheeling, W. Va., may be taken as typical of the existence of an open steel market in competition with the Steel Corporation. That company had, during the ten years following the organization of the Steel Corporation, increased its finished product of billets, sheet bars, nails, tubes, plates, skelp, and sheets largely over 400 per cent, and its market covered the entire country, Mexico and Canada. Its sales manager said that their competitors are all the leading steel companies, pretty near, take the Lackawanna, Cambria, Republic, the Youngstown Sheet & Tube, the Wheeling Steel & Iron and the various constituents of the Steel Corporation. The prices which they obtain for their steel products are not fixed in

agreement with their competitors. That is true of each and every year of the ten years that he had been general manager of sales. It is true of each and every article they have produced and sold in the market. There has been no time during the ten years when the price of any article they have produced and sold has been fixed by agreement with any competitor. He is able to say that because the chances are that if it had been done in his company he would have known it. That is his business. The prices have sometimes been fixed in a general way in consultation with their president. *No price has ever been suggested by the president or anybody else in any of these conferences, as a price agreed upon by any competitor.* The considerations that controlled him in these conferences, or when he acted independently of them in fixing prices, were competitive conditions and cost of manufacture. The state of their order book affects the question of prices. When the order book is lean, they probably make lower prices. When full of orders, the chances are they will advance prices. That is always the case. It is observable that competition is keener and competitors more active when times are dull and order books are lean. Prices usually rule higher when business is active, and when business is dull they rule lower. The prices obtained by them have fluctuated. He would say the prices obtained by their competitors have fluctuated. The trade or competition in these various articles manufactured has been nearly always active during the period he has had charge of the sales. The competition has been what you would term keen. They met three or four or more competitors in every article they manufacture. The competitors are numerous. They have grown in numbers and output.

The testimony of the chairman of the Republic Iron & Steel shows how that large company arrives at its prices; they do not have uniform prices. They sell to some customers at one price and to other customers at another, varying with the size of the order, the quality and the character of the service they are expected to render naturally. They have traveling men and their own branch sales offices. As a general rule, they send out to them prices at various times at which they are to sell their

various products. They give minimum prices below which they shall not go, and allow them to use their intelligence in getting all above they can. That minimum would naturally be the same for all of them. Generally speaking, it would be the same based on cost. They give them the same latitude; in other words, the same general base, which represents a minimum below which they must not go as it might involve a loss.

As to the Jones & Laughlin competition, the testimony of the man in charge of the sales is that Jones & Laughlin make steel billets, slabs and blooms, and convert these into finished products, principally structural material, plates, bars, shafting, chains, spikes, wire, wire nails, tin plate and black sheets in tin mill sizes. These different products that they have are sold in competition with other makers of similar products. The competition is unlimited. He means unlimited by agreements as to prices. That is true of everything he has mentioned. *He says that this has been so to his knowledge for about nine years.* The competition has been keen. It extends to competition in the matter of prices.

Turning from fellow competitive makers of the same general products as the Steel Corporation, we naturally turn to the testimony of millowners who use as their basic supplies the products made by these large companies and inquire whether, as buyers, they have found any price fixation by these basic manufacturers. As a type of that character, we note the testimony of the president of such a company who, in substance, says:

I should say we were using about 25,000 to 30,000 tons a year in 1901. It has been growing each year. I think last year we purchased something in the neighborhood of 100,000 tons. I know of no other single customer for bar mill products in the United States that buys as much as 100,000 tons. We buy from the Carnegie Steel, the Cambria Steel, the Republic Iron & Steel, the Youngstown Sheet & Tube, and others. We have always found competition for our purchases of bars. Very keen most generally. Of course, there are times in normal business when it is not so keen, times when the consumers of bars are competing to get them. We can generally purchase at a less price than the quotation. That is, the quotations published in the *Iron Age* or the *Iron Trade Review*. *I have never*

observed any indication of a combination or agreement among bar makers to fix prices. We have always been able to buy on fair competition. I think we have always been able to get the benefit of fair competition.

We have carefully and patiently studied the voluminous testimony varying on the general course of all branches of the steel trade covering the whole time the Steel Corporation has been engaged in such trade. The testimony, as noted above, runs from volume 18 to volume 28, inclusive. It covers proofs by its manufacturing competitors in all branches, and also the different classes of customers whose trade it and its fellow competitors seek. It is apparent that among this latter class (that is, the consumers of its products) we would naturally find evidence of any throttling of competition, of any undue restraint of the steel trade. The typical extracts we have made above from varied sorts of buyers, of varied sorts of products, cover wide ranges of consumers. No one can read these volumes of testimony and fail to be satisfied that this great body of business men, scattered over all parts of the country, in keen competition with each other in their several lines, is alert in seeing that competitive conditions exist between the manufacturers of basic steel products from whom they buy. And the sworn testimony of these men, who are vitally interested in the maintenance of real competition between the Steel Corporation and its manufacturing competitors, that such real competition does exist and has existed during the past ten years, cannot but carry a conviction that such is the case. A study of the testimony of these men, who are close to and vitally interested observers of the prices of these products, shows that a single large concern, by lowering the price of any substantial steel product it sells, can depress the obtainable price. It further shows that the converse is the case — that no single large concern, by raising or even maintaining the price of any substantial steel product, can raise the obtainable price. It further shows that the prices at which actual sales were made during this time in the steel trade depend on whether the consumption of steel was such that the mills were crowded with orders from buyers, or whether buyers

were crowded with offers from mills. In other words, if the mills were crowded with orders, there was an increase of competition between buyers and a corresponding decrease in competition between manufacturers. On the other hand, if the mills were lacking in orders, then there was a keen competition between mill men to get orders and corresponding decrease in competition among buyers to give them. The proofs further show that, when there is an increase of orders and a stiffening of prices, steel buyers are apt to buy at once, and this tends to further increase the price, but, on the other hand, buyers are not apt to buy at once when the price grows less, but wait until the bottom is reached, and this withholding of orders tends to accentuate the fall of prices. The proofs further show that in normal times, when ability to fill orders and ability to get orders are in fair balance, prices vary but little, but, as soon as that balance is disturbed, the tendency of prices up or down becomes accentuated, and increased competition follows between the mills, if prices go down, between buyers, if they go up. The study of these proofs, given by both mill owners and buyers of their product, satisfies us that this has been and is the course of the steel trade, and we are therefore justified from the proofs in concluding that the prices at which steel products have been bought from the Steel Company and its competitors have been fixed by business conditions — overdemand or oversupply. The proofs also show the same conditions and results prevail in the European steel market.

Assuming, then, that the iron and steel trade in the United States is and has been during the time here in question flowing in the natural and normal channel of demand and supply and of genuine competition, we next inquire as to what course the proofs show the Steel Company pursues in reference to such trade; in other words, is its course one of monopoly or in restraint of trade? Let us first ascertain what the practice of the Steel Corporation actually was and is as to prices. Whether that course be right or wrong, whether it be in violation of the letter or spirit of the Sherman Law, there can be no uncertainty in three things: First, what its policy is; of its having been openly and publicly avowed; and, lastly, of its having been

followed. Its avowed general practice in regard to prices is thus summarized by its chairman, Judge Gary, who says:

> The United States Steel Corporation has endeavored; so far as it could, to prevent the unreasonable increase of prices. It has been a decided factor from time to time in keeping prices down to a level which was believed to be fair and just. Prices generally are controlled very much by the business conditions of the country. The ordinary laws of trade and supply and demand fix the general prices of commodities, but the Steel Corporation has endeavored to prevent sudden and violent fluctuations downward by its advice, but more particularly by its own action in fixing its prices, and has endeavored to prevent the unreasonable increase in prices at times when the demand was greater than the supply and there was a general disposition in the trade to take advantage of these conditions and unduly increase prices.

That it has followed this policy is the testimony of both its competitors and customers.

The fact of such policy and the reasons for it are thus summarized by Charles M. Schwab:

> While I was president of the Steel Corporation, I should say that our prices as a rule were somewhat above the other prices in depressed times and below the other prices in prosperous times. In other words, we endeavored to keep more uniform. . . . The theory was that many smaller dealers bought their steel from this corporation; that we did not want them to be speculators, nor did they want to be speculators, as it were, in the price of steel; that as a rule they were caught with big stocks when prices were high, and made heavy losses by reason of rapid reductions and the inclination to overbuy when prices were low; and, if prices were kept nearly uniform, people buying steel would buy for their requirements and not speculatively.

The proofs also show that this policy, which is also followed by other large steel manufacturers, largely resulted in doing away with what are called delivery premiums; that is, of postponing deliveries of orders already taken at lower prices and giving the preference to orders taken later at higher prices, which higher prices were in effect obtained under the guise of so-called delivery premiums. The proofs likewise show that the lessening of extremes in the prices of basic steel products greatly

benefits mills and factories that further fabricate such articles. Thus one such witness testified:

> Of course, I am only a small manufacturer and perhaps to a certain extent typical of the average small consumer of steel products, but the conditions in the present decade are far more stable and far more favorable to intelligent manufacturing than they were in the previous period. Of course, the fluctuations have been less, and you can calculate on your road which you have to go over with a good deal more certainty. . . . The sudden fluctuations, rising and falling in prices, were very unfavorable to the maintenance of contracts or to intelligent manufacturing. One could not buy and be sure that he could get out with a profit on account of the dips in the market.

The proofs show that the practical effects of this policy are that in prosperous times buyers are apt to buy from the Steel Corporation and in depressed times from its competitors. Whatever the wisdom or unwisdom of such a policy may be, we find no proof tending to show that it tends to monopolize the steel business or to unduly restrain trade or to prejudice the public. There is no proof that it in any way interferes with the right of any other person in the steel business to fix his own price on his own steel product. The proof shows that the Steel Corporation, in the exercise of its own business judgment, has elected to publicly announce its prices, to adhere to them with all buyers alike, and to give timely notice of its purpose to change them. It is neither the duty or the province of this court to express any opinion upon such policy, unless we are satisfied, as laid down by the Supreme Court, "that it prejudices the public by unduly restricting competition or unduly obstructing the course of trade," and of this we have no proof. For, as we have seen, the testimony of those engaged in the steel trade is that this policy of the Steel Corporation, in refusing to raise prices, has not restricted competition or obstructed the course of trade, but, on the contrary, has tended to prevent prices from rising to what was aptly termed a "runaway market." And in this connection it is just to note that if the Steel Corporation, in refusing to advance its own prices, prevented other manufacturers from advancing theirs, it was only exercising a veto power, which every one of many other competitors possessed,

and was following a policy which was also followed by other large competitors who were also opposed to advancing prices. It is also just to say that in giving timely notice of its purpose to change them, and in giving publicity to its prices, in adhering to them, it will be seen on reflection that the Steel Corporation has adopted a policy of price publicity and adherence, somewhat analogous to the freight rate stability followed by the railroads under the directions of the Interstate Commerce Commission, which published their rates and only changed them on notice.

We now turn to the other phases of this policy, viz., the corporation refusing to sell at lower prices when prices dropped. That it did so, and that by reason thereof it lost business, which naturally went to those who did lower their prices, the proofs abundantly show. Of its right to refuse to sell at lower prices, provided it does not force others to do the same thing, there can be no question. This brings us to the question: What was the policy of the steel trade prior to 1901 under such conditions, what was its result, and what evils are avoided by this change of policy?

In that regard, the testimony leaves no doubt. We take the Carnegie Steel Company's course in the earlier steel period as illustrative, not only of its policy, but as fairly typifying that of its competitors as well. The cause of falling steel prices is, of course, that there are not enough orders to cover the production, and this leaves two courses open to the steel manufacturer: He must either shut down his mill or go after orders to keep it running. The policy of the Carnegie company (and in that respect it was the same as others) was to try to keep the mills going, no matter what price they got for their product, or no matter whether their getting such orders meant the complete stoppage of their competitors' mills. Practically applied, this policy meant a fierce, ruthless price-cutting trade war, the practical results of which were that, if these low prices enabled one company's mills to get the orders to run its mills, the taking of these orders from other companies' mills and other sections of the country shut them down. Thus, in the Government Exhibit we find a letter from Mr. Carnegie to the Carnegie Steel Company, embodied in its minutes, reciting such policy:

In the former depressions we announced our policy, viz., take all orders going and run full. Our competitors believed we meant what we said, and this no doubt operated to clear the field. One after another dropped out; finally Pennsylvania Steel dropped out and only a few remained who could meet the lowest prices.

Another letter of Mr. Carnegie to his company is given in evidence in which he says:

My view is that sooner or later Harrisburg (Pennsylvania Steel Company), Sparrows Point (Maryland Steel Company), and Scranton (predecessor of Lackawanna Steel Company) will cease to make rails like Bethlehem (Bethlehem Steel Company). The autumn of last year seemed as good a time to force them out of business as any other. It did not prove so. The boom came and cost us a great deal of money.

The policy of taking orders, even without profit, was the destructive competition of that era. "To keep running, not to make profit, is the point we should steer to," was the direction to the Carnegie Steel Company. "Take every order, otherwise we come to a stop and only feed competitors who would close if we went to rock prices." Such being the policy, the proofs leave no doubt as to its effect. Mr. Schwab testified: That the destruction of the small and weak (competitors) was a practice not unknown in the old days. It was rather extensively carried on. It was at times with quite effective and marked results. That he did not know what percentage of them emerged from the steel wars in the old days. Not many. There were more gravestones than live competitors. That they did everything they could to secure all the business they could secure, regardless of the price at which they secured it. That it was pretty hard on the competitors at times, but that was their policy and one that it was very difficult to break away from.

Referring to one of these ruinous trade wars between two large steel companies, Powell Stackhouse, president of the Cambria Steel Company, which was not one of the participants, testified:

Q. How nearly can you fix the time of what you called the Gates and Carnegie row?

A. That was somewhere in the '90's; in the latter part of the '90's.

Q. About 1897, or somewhere along there?

A. Somewhere along there; from 1895. I would not be sure of that.

Q. And that was followed, I judge, from what you say, by rather a fierce trade war lasting a year or two?

A. Yes; in all lines of steel.

Q. In all lines of steel?

A. Yes, everything. As a result of that, there was the keenest competition and steel was sold, bar steel, at, I think, less than nine-tenths of a cent.

Q. And it cost more than that to make it?

A. Yes; a good bit more.

Q. And the consequence of this was very serious to trade, was it not?

A. It was serious to everybody in the trade. It was very serious, for instance, to the warehousemen, that had some thousand or more tons of steel, or whatever they might have on hand. Their stocks were probably reduced from one or two cents a pound way down.

Q. That warfare left a trail of ruin?

A. Yes; it did.

Q. There were a great many failures on account of it?

A. Yes.

Q. And general business disaster?

A. General depression.

Q. And business disaster?

A. Yes, sir.

Q. And failure and bankruptcy?

A. Yes, sir.

Q. (continuing) — were the direct effect of it, were they not?

A. Yes.

Q. You had had trade wars before, I suppose, had you not?

A. Yes.

Q. But none so severe as that?

A. None so severe as that.

Q. But they were always attended with injury to the business, and especially to the warehousemen or middlemen, were they not?

A. Yes, sir. The middleman had bought and had his material on hand, and, overnight, by the price falling a few dollars a ton —

Q. (interposing) He was ruined?

A. He was ruined in some cases. Some of them carry very large stocks.

Q. The effect, I suppose, of such warfares, and particularly the Gates and Carnegie warfares, was felt mostly by the weaker concerns in the business?

A. We all felt it.

Q. You all felt it, but the stronger ones weathered it?

A. Certainly.

Q. And the weaker ones all went to the wall?

A. They were weakened so that they gradually dropped out.

Q. They gradually dropped out?

A. Yes, sir.

Q. So the effect of that was not confined to the manufacturers, but was felt even more by the warehousemen and jobbers, was it not?

A. Yes. They could measure their loss at once. If they knew what their inventory was and the difference between what they paid and what prices had fallen to, they could measure their loss at once.

Q. What about the retailers? What was the effect on them?

A. The same thing. Anybody that carried a stock of steel or iron on hand, if the value of that stock was reduced $5 or $10 a ton, just simply had to write off that amount.

Indeed, the general competitive policies of the steel companies toward each other is well summarized by the chairman of the Steel Corporation, who says:

On the other hand, in olden days, the rule in this country was different in this line of business. I have no doubt the suggestion of Mr. Carnegie, which was read in court a few days since when I was present, represented not only his views. but the views of his associates, and the views generally held amongst those who were in charge of the iron and steel industry of this country. There was a competition that was bitter, fierce, destructive. If it did not absolutely drive competitors out of business, it so harassed and injured them as to prevent them from extending their business, or from taking advantage of their location, and at times compelled them to close their mills, discharge their employés, and disrupt their organization, and, in fact, was a competition that, in the opinion of those in charge of the United States Steel Corporation, I might say the opinion of those in control of the industry generally in this country at the present time, was calculated to destroy, to injure instead of build up, to prevent extensions of trade, to limit the capacity or the opportunity of many who were engaged in the trade.

And in that connection it should be noted that no testimony has been produced in this record that a return to the old trade war system of ruinous competition would, as a matter of fact, benefit the public interests. On the contrary, the proof is that present business methods and ethics are more to be desired. As expressive of the view of those in the steel business who are not connected with the Steel Corporation, we may note the testimony of the president of one of the largest steel castings companies in the country, who says:

Before the formation of the Steel Corporation, business ethics, I might say, were in very bad shape; competitors had no confidence in each other; they resorted to subterfuges, misrepresentation, and false statements. That same lack of confidence existed between sellers and many purchasing agents. It was a very undesirable condition in which to do business. For the past seven or ten years (in later times, at any rate) all that misunderstanding or misgiving has been displaced by manly, straightforward dealing. I do not think it could have been brought about without the Steel Corporation's influence and example. The benefit of that example has extended into collateral industries like ours. I have noticed an improvement in the competition of our own business in an ethical way. We still have the competition, but we do not try to misrepresent or tell lies any more. We are honestly friends now. Then we pretended to be friends, but were the bitterest enemies. It appears to be an improvement that pervades the entire steel line, and being the largest unit, the most influential unit, and setting a commendable example, has led us all to realize that it is a betterment.

A study of these proofs satisfies us that, apart from all ethical questions, the strong trend of the steel business at the close of the last century was toward driving competitors out of business by cutting prices, and that the business policy inaugurated by the Steel Corporation, and in which policy its competitors subsequently followed, has resulted, in the ten years of its existence: First, in a more general division of business between all competitors in the steel business than under the older system; second, in tending to minimize the shutting down of its own and its competitors' plants in times of depression; third, it has made steel products nonspeculative, and has therefore benefited all dependent iron and steel manufacturers by enabling them to

have a steady, nonspeculative supply of those basic steel products on which their plants depend for operation. The evidence on which these conclusions are based is corroborated by the business facts and business results which we now summarize in the working out of this policy for ten years by the Steel Corporation and its competitors. During that time the business of both competitors and steel company has increased very largely, but it is highly suggestive, indeed, conclusive, proof that the Steel Company had neither monopolistic control or power to restrain trade, since the proportion of trade increase was very materially greater on the part of the Steel Corporation's competitors than its own. These significant figures prove that mere size, or bigness of business, is not necessarily a monopoly of business at the expense of all others engaged in it. And in that connection, and as aptly expressive of our views, we may quote with approval the language of Judge Hook of the Eighth Circuit, in his concurring opinion in the Standard Oil case:

> Success and magnitude of business, the rewards of fair and honorable endeavor, were not among the evils which threatened the public welfare and attracted the attention of Congress. But when they had been attained by wrongful or unlawful methods, and competition has been crippled or destroyed, the elements of monopoly are present.

In the most important element of steel rails, an item on which great stress has been laid as a most important factor of monopoly, and control of prices, we find that, in spite of the general increase of rail production, the Steel Corporation's relative proportion of rail business has fallen off nearly 8 per cent, while its competitors have increased correspondingly. In the great basic item of steel ingots, on which the great bulk of steel manufacturing rests, while the Steel Company's ingot business increased 44 per cent, its competitors' ingot business grew nearly three times as fast, viz., 137 per cent. To say that any monopoly of ingots existed when this bill was filed, that it now exists, or that it can exist, is simply to run counter to the testimony of ten years' business experience and to the evidence in this record. In the great item of structural shapes, which

enter into bridges, building, and other common uses, while the business of the Steel Company in these years increased nearly one half, to be exact 42.7 per cent, its competitors have, during these years, gone ahead nearly four times as fast, 164.4 per cent, and in that connection it will be observed, as heretofore shown, that a large part of the increase of the Steel Company's structural product was in the foreign, not in the home, market, in which latter market it has more than 300 fabricating competitors. Practically the same proportions exist in wire rods, the basic of wire fences, and other articles of widespread use. In wire rods, the Steel Corporation has increased its business 49.7 per cent; its competitors 182.2 per cent, nearly four times as fast. So also a monopoly of the tin plate industry was feared, while the outcome shows the Steel Corporation has in tin plate and terne plate increased 63 per cent, its competitors have increased threefold as fast., viz., 186 per cent. So in the pipe industry. Instead of there being a monopolistic and exclusive growth, there has been a relative retrogression, for while the pipe business of the Steel Corporation has largely increased (in wrought pipe 36 per cent and in seamless tubes 100 per cent), its competitors have increased nearly six times as fast (in wrought pipe 209.9 per cent and in seamless tubes over seven times as fast, 750 per cent). In the item of pipe alone, it has already been noted in the testimony of the general manager of a great gas company that, as a buyer of pipe, it enjoys active competition between 13 concerns.

These facts and figures conclusively answer the charges of monopoly and restraint in the home market. We are therefore justified in answering in the negative the question to which the foregoing part of this opinion is addressed, namely, Was the United States Steel Corporation, at the time this bill was filed, then prejudicing the public interests by unduly obstructing the steel and iron business of the United States?

We turn next to the steel and iron trade with foreign nations and address ourselves to the second question, namely, Was the United States Steel Corporation, at the time this bill was filed, then prejudicing the public interests by unduly restricting or unduly obstructing the steel and iron business with foreign nations?

In taking up that question, it is to be noted that the entire foreign business here in question is now carried on, not by the Steel Corporation, but by a subsidiary of the Federal Steel Company called the United States Steel Products Company. This company was formed in 1903, and the Federal Steel Company is the owner of its stock. This Products Company is not made a party to this bill, and there is no prayer for its dissolution. All other subsidiary companies of the Steel Corporation are made parties, and their dissolution in many cases prayed for. Whether the omission of the Products Company from the bill, and the absence of any prayer for its dissolution, was an omission, or was advisedly done, with the purpose of conserving its foreign trade, does not appear. But the absence of a formal prayer for the dissolution of the Products Company is, however, of no practical importance, for the continuance of such foreign trade of the Products Company is manifestly dependent on the manufacturing facilities, the product diversity, and the financial ability of the Steel Corporation. If, therefore, the Steel Corporation be dissolved by this court, the Products Company will be divested of the practical commercial power of continuing its foreign trade, since the proof is that 80 per cent of the goods it sells necessarily comes from the Pittsburgh district in which the Federal company has but little production. If the Federal company be also dissolved, then the Products company will, of course, be left without any mills or plants which are so located as to do export business, but 2 per cent of the Federal Steel Company's product now going into foreign trade. So that the foreign trade of the Products company, if acquired and held in violation of the Sherman Law, can be as effectually ended by a dissolution of the Steel Corporation, or the Federal Steel Company, as though the Products company had been made a party to this proceeding and its dissolution prayed for and decreed.

It is apparent that the monopolization and restriction of foreign trade must, in the nature of things, consist of either taking away from others a foreign trade which already existed, or if such foreign trade was not in existence, then in building up or maintaining such foreign trade by preventing or restraining others from entering it.

Now foreign trade is not a mere general, theoretical abstraction of selling abroad, but is a concrete, definite, commercial business proposition in iron and steel. We have our domestic trade, which consists in supplying domestic use or consumption. And such domestic use necessitates one having or taking to the market where his customer is located the articles the latter wants to buy. It goes without saying that if one man has a wire mill at Pittsburgh situate near another man's billet mill, and that billet mill has in its warehouse at all times an ample supply of billets to run the wire mill, (the proofs show 18 different analyses of such billets are required), the wire mill owner will prefer to deal with, and will deal with, the billet mill in Pittsburgh in preference to dealing with one at Chicago. And this is so, because freights are eliminated; uncertainties of railroad transportation are avoided; if materials prove faulty or not of the right metallic character, the mischief can at once be remedied. Of course, if the Chicago mill, from any motive, chooses, either from overproduction, business needs or other causes, to offer the wire mills at Pittsburgh, billets at a lower price than the Pittsburgh mill, a sale might be made; but this occasional purchase could and would result in no established, normal trade between the Chicago billet mill and the Pennsylvania wire mill. The only way such normal trade relation could be established would be by the Chicago manufacturer locating a permanent stocked warehouse near the Pittsburgh wire mill. If its cost of production was so low and it could pay the freight from Chicago to Pennsylvania, and could furnish in quality, quantity and price the same product as the Pittsburgh mill, then, and then only, could it hope to have normal, continuous trade with the Pittsburgh wire mill. We take this homely but suggestive illustration to emphasize what the proofs show are the demands and requirements in foreign iron and steel markets which confront an attempt to enter them, and that such market is not to be held by the mere occasional shipping of goods to foreign countries. Moreover, in considering the possible range of foreign iron and steel markets for American iron and steel, there must first be excluded from that market, Germany, France, Austria, Italy and Russia. The proof is that the tariffs of each of those

countries prevent the sale there of American iron and steel. The proofs also show that the attitude of the English public and the hostility of English labor organizations toward American iron and steel likewise prevent American iron and steel products entering England, save wire fences, the manufacture of which is only now being taken up there. It follows, therefore, that the iron and steel trade of the United States with foreign nations must be largely built up in other parts of the world, and such has been the outcome of the efforts of this company as shown by the proofs. Referring to trade in such nations as are not closed to the iron and steel business by their tariffs, these in a general way are the steel markets of Asia, Africa, the British Colonies, all South America, Cuba and Mexico. But while these markets are open, they were, when the Steel Corporation was formed, "practically preëmpted by foreign manufacturers and foreign merchants; that is, principally continental concerns, English concerns, as well as having branch offices and warehouses in all of the consuming markets of the world. It was a very difficult thing to enter those markets. The European manufacturers had been established in the markets of South America, Asia, Africa, and the Orient, some of them over 50 years. There was not only a prejudice, but a hostility, in most cases against newcomers in the trade. In order to get a foothold in these markets, we usually had to sell below the prices of the concerns that were established there, and who had their customers and native salesmen, and all the advantages that go with a long occupation of a business in any foreign country. It is more the custom in foreign countries than it is here for people to attach to themselves customers that buy from them regularly."

Moreover the proofs show, and such would seem to be the manifest commercial fact that:

It is impossible to develop a foreign business unless it is done continuously. Buyers will not patronize people who are not in a position to give them a continuous source of supply.

Without entering upon a discussion of other matters, it suffices to say that, not only were these foreign markets preëmpted and tenaciously held by foreign manufacturers, foreign merchants

and foreign bankers who refused to finance importing enterprises there unless there was a stipulation that all materials should be bought in such bank's own country, but the markets required the maintenance of varied lines of products, the only way to supply which varied lines was by maintaining varied lines of finishing mills at home and the maintenance of large warehouses abroad. The proofs in the case show that in 1901, when the Steel Company was formed, with the exception of wire exportations — which for various reasons was not broadly successful — there was no iron and steel trade of an established or continuous character between American iron and steel manufacturers and foreign nations. It is true there were spasmodic exports which at times amounted to considerable volume, but they were not continuous or sustained, and they resulted in no established trade or dealing. Indeed, in many cases the nature of this spasmodic trade was such as to create a hostile feeling toward any subsequent effort on the part of American iron and steel trade to enter the same foreign market. The proofs show that at that time and for many years previous, so long as the demand of the home market was sufficient to absorb their product, our iron and steel manufacturers made no effort to sell their output abroad. When, however, the reverse was the case, and they had on hand a surplus product for which there was no domestic trade, they went into the foreign market and tried to get rid of such surplus product there. The European and American steel and iron market being interrelated, the proof is that, in addition to paying the freight to get his goods to the foreign market, the American manufacturer had, in order to get customers away from the foreign manufacturers who were already in possession of such trade, to cut the price when they sold in the foreign market. This spasmodic course grew to be known in the steel business as "dumping," and may be well likened to the bargain sales by which a merchant seeks to dispose of a surplus stock which he cannot sell at normal prices. It will, of course, be obvious that a manufacturer could not continue such low-price dumping any more than a merchant could dispose of all his stock — instead of his surplus stock — at bargain prices. The proofs show the same course of dumping abroad in times of depressed markets was

followed by European steel manufacturers in our market. The then status of American steel manufacturers is shown by the proven experience of the Carnegie Steel Company. It was the most aggressive of any of the steel companies to enter foreign trade, exporting 70 per cent of the then steel exports. The Carnegie Company's location, facilities and freight rates enabled it better than most other companies to enter foreign trade, and from its works, as the foreign trade of the Steel Corporation developed, such trade to the extent of 24 per cent of the entire product of the Carnegie Company goes into such export trade. It will therefore appear that the Carnegie Company can be fairly regarded as the best fitted of American steel companies to compete for export trade. Referring to that time, the president of that company testified:

> We had made spasmodic attempts at it. In dull times when business could not be secured at home, we would make attempts at foreign business by going in and making an unusual price, which was the only way that any foreign business could be secured then, inasmuch as we had not an established business or business connection, and therefore customers were not inclined to buy from a firm who could only furnish them occasionally.

The relation of the Carnegie Company to foreign trade is shown by its minutes. From the proofs in the case three things seem settled, namely: That when the steel Corporation was formed American steel manufacturers had no real dependable export trade abroad; that such sales as they made were spasmodic, made with a view to dumping surplus product; and such sales were secured by underselling the European market when they had no home market. It will also appear that being excluded by the steel tariffs of Germany, France, Russia, Austria and Italy, and by other causes from England, such dependable foreign markets as were open for them to build up, as will be seen later, had to be found in other parts of the world. This summary of the situation is warranted by the study of the proofs.

Seeing, then, that when the Steel Corporation was formed, no such volume of foreign trade in steel existed; that the acquisition of any part, or indeed the whole of it, could constitute

a restraint of trade with other countries; and seeing that the foreign trade which the Steel Corporation had during its earlier years had increased from approximately $31,000,000 to $91,000,000 — we turn to the next question, Did the Steel Company acquire this original or additional trade by monopolizing or restraining foreign trade, or attempting to do so; or, on the other hand, was its acquisition the natural and normal growth of fair business effort? We have said the foreign trade of the Steel Company in 1911 was $91,000,000, but of that amount some $30,000,000 is really not solely its own, but was shared by it with other American steel manufacturers. To explain, it will hereafter appear that in the development of a foreign steel trade, the Steel Corporation has established agencies, warehouses, freight communications and other exporting agencies in many of the markets of the world. As we read the testimony, in reference to this $30,000,000 of foreign trade, it seems that if an American manufacturer of steel finished products, for example, locomotives, oil tanks, gas tanks, cars, etc., had an inquiry, or desired to make a bid to furnish such goods in some foreign country, where such manufacturer did not have, but the Steel Corporation did have, a representative, the Steel Corporation would, on request, ascertain and report to the American tank manufacturer what price he would have to put on his tanks, etc., to get into the desired foreign market. The ability of the tankmaker to meet such foreign competitive price in the prospective buyer's market depended, amongst other things, on two items — the cost of the sheets from which his tank was made, and the freight cost of delivering the tank. In case the current prices of such sheets in the American steel market were such that the tankmaker could not sell his tank low enough to compete with the foreign bidder the Steel Corporation would agree to furnish the plates at such lower price as would enable the tankmaker to underbid his foreign competitor. This price reduction, coupled with the fact that the Steel Corporation would forward the tanks with its own freight, enabled the tankmaker and the Steel Corporation to thus jointly sell the tank, which neither could do alone. By such operations, where it made the basic material, but did not make the finished article,

the Steel Corporation, in 1911, thus did $30,000,000 in trade abroad in finished steel products in coöperation with other American manufacturers. The proofs show that this course of price reduction was followed in order to induce American manufacturers of finished steel products to coöperate with the Steel Corporation in extending the latter's foreign trade. The uncontradicted proof in that regard is that these foreign reduction prices thus given to American manufacturers to enable them to compete in the foreign markets were "open to all comers; anybody that wanted to develop a foreign business received our assistance, not only in the way of special prices, but we would lend him a salesman in a foreign country and place our office at his disposal and help him in every way to build up a foreign business. . . . Our office is an encyclopedia for the manufacturers of the United States, particularly in iron and steel and those collateral lines. We have never hesitated to give information with regard to conditions in countries, and the credit of people whom we may have been doing business with, and especially facilities and information generally with regard to tariffs in countries and railway facilities for internal distribution generally. . . . I had prepared under my direction a list, I think, of about 158 manufacturers to whom we have made a special allowance in order to enable them to develop a foreign business."

The proofs show that this large volume of business, termed by the Steel Company "reëxport" business, and amounting, as stated, to $30,000,000 in 1911, was shared in by 158 other firms or companies, and in making such reëxport articles from 15,000 to 18,000 men were employed. The proof is that on ocean freights the Steel Corporation had no rebate or advantage over its competitors. It will be observed that in thus reducing the price of basic steel materials to enable manufacturers to enter the foreign markets, the Steel Corporation has pursued the same helpful course of lower freights for exports which the Interstate Commerce Commission has, since 1903, approved of the railroads doing. In that regard the proofs show if a shipment is made from Pittsburgh to New York under a bill of lading beginning and ending with Pittsburgh and New York, that

where it is known that it is going to be exported the rate is less than when it is known it is going to stop in New York; the tariffs are published. . . . There is an export rate and a domestic rate, and the government has encouraged the export business to the extent of permitting the Interstate Commerce Commission to make export rates. The export rates have been in effect since 1903.

And we may add the proofs show that the Interstate Commerce Commission has gone to the extent of differentiating among different articles for export, making freights on export rails lower than on other export articles. We may here say that the Interstate Commerce Commission and the railroads in thus coöperating with the Steel Corporation, and these other manufacturers in allowing lower freights from interior points to the seaboard on goods intended for export, have followed the policy adopted in European countries. In that regard the proofs show:

The German government and the German railroads help for the export of finished products, but they charge the full domestic rate for any finished product that is imported.

Passing on, then, from this $30,000,000 of the foreign trade which the Steel Company has created for itself by inducing domestic consumers of its basic products to jointly enter into a foreign trade, and considering the other foreign trade, $60,000,000, which is its own, we examine the evidence as to whether the creation and building up of this, its own foreign trade, involves monopoly or restraint of trade. This becomes all-important, because the Steel Corporation contends that the creation and building up of a foreign steel and iron trade was one of the controlling reasons that led to its formation, and not a purpose to restrain or monopolize interstate home trade. In that regard the contention of the Steel Corporation is that no such foreign steel and iron trade could be built up without the large resources of the Steel Company, and the varied products which the integration and combination of its units alone made possible. The mere statement of this contention shows its importance, for if the twofold purpose of this statute is to foster

and protect trade, both foreign and interstate, and if foreign trade cannot be increased without some such mechanically varied and financially strong agency as this Steel Corporation, then manifestly such agency is not a violation of a statute whose purpose was to permit — not to prevent — the normal, natural and to be desired development of unrestrained, unmonopolized trade, both foreign and domestic. In taking up this question, we dismiss once and for all the question of mere volume or bigness of business. The question before us is not how much business was done, or how large the company that did it — the vital question is, how was the business, whether big or little, done — was it, in the test of the Supreme Court, done by prejudicing the public interests, by unduly restricting or unduly obstructing trade? The question is one of undue restriction or obstruction of trade, and not of undue volume of trade. If mere size were the test of monopoly and trade restraint, we have not one, but a half dozen unlawful monopolies in the large department stores of a single city. If a manufacturing and selling business, fully equipped for its local market, extends its operations to cover a state, its business, its facilities, its capital, must grow larger. If it is to cover nations, it must be larger still. These plain facts simply buttress the holdings by courts that the normal and necessary expansion of business to any size is not forbidden by the Sherman Law, unless such expansion is accompanied or accomplished by an undue restraint or obstruction of trade.

Turning, then, to this foreign trade, we find that in 1901 the Steel Corporation did a foreign trade of $31,000,000, and in 1911 of $91,000,000. This was 90 per cent of the foreign iron and steel trade of the country. On the one hand, it is charged that this foreign trade was acquired by violation of the Sherman Act; on the other, that it is the normal and natural result of lawful business, commercial foresight and persistent effort. To determine these contentions from the evidence, we now address ourselves. Of the purpose of this corporation to create and possess this foreign trade, there can be no question. So that, if it was illegally done, the company cannot escape the legal consequences. Its avowed purpose to enter into and ac-

quire foreign trade in iron and steel is shown by the corporation's own proofs. Indeed, in outlining the plan and scope of the operations of the Steel Company, whose formation he was then advocating, its first president says:

I enlarged and perhaps made a more strenuous talk to Mr. Morgan upon the subject of export, and our ability to export, and foreign business in foreign markets, than any other, excepting only the economic advantages to be derived.

The fact that the development of the foreign trade necessitated a wide diversity of products, that this product diversity was to be obtained by the Federal Steel Company acquiring a number of mills making such diversity of products and completely integrating itself, is shown by the proofs.

And that such foreign trade demanded such wide diversity of products as could only be supplied by a company which was broadly integrated to manufacture such diversified supplies is shown by the proofs. In that regard, a witness of long experience in foreign trade says:

Q. What is the nature of your customers in foreign countries? Do you sell merchants or directly to consumers, or both?

A. We sell to merchants, consumers, and manufacturers.

Q. Is there any advantage in selling to merchants to have a diversified line of product?

A. A great advantage. That is the reason why we have been able to develop our business, because we could offer them a diversified line of products from one source.

Q. From your knowledge of the business and of the way it is done, what would you say as to whether or not the different constituent members of the Steel Corporation could all together have developed such a foreign trade as has been developed by the corporation, if they had remained separate and distinct?

A. It would have been utterly impracticable or impossible. We had had an exemplification of that at the Pittsburgh Wire Company, where we were obliged to confine our exports to two or three different products, because of the necessity of having facilities to deal with certain lines of business. . . .

Q. Take, for instance, the American Steel & Wire Company, as an economic proposition, as a business proposition; will you state

whether or not it would have been feasible, or possible, for the American Steel & Wire Company to maintain agencies in the various countries as stated on Exhibit 39?

A. It would have been impossible owing to the cost.

Q. What would be the fact as to the Carnegie Steel Company in all these countries?

A. The same thing would apply to the Carnegie Steel Company, even to a greater extent because of the character of their product, which is not as widely consumed as wire products and sheet steel products, and some of those others except in the case of some coarse products.

Q. What influence, if any, does the offering of one class of steel products have on the sale of another?

A. In the export markets, we say that one product sells another; that is, by having the great range of products, the buyer has an opportunity to order practically all of his requirements. Frequently these people will charter their own sailing vessels and load them themselves. They want to buy everything they can.

That this is a correct business estimate of the demands of the foreign market is corroborated by the testimony of the president of probably the most widely diversified range of finished steel products company in this country, who says:

Q. In what way has your ability to carry on a foreign business been affected by the fact that you have a full line consisting of many kinds of edge tools and cutlery?

A. Without that, we would have practically no business abroad.

Q. Why is that?

A. Because no one line or one item in the line would be sufficient to interest the foreign buyers. It is the completeness of the line under one brand and one uniform quality that they seem to take an interest in.

Q. That is, they buy full lines of you, do they?

A. Yes, sir.

Of the fact that this policy of foreign trade expansion was as such entered into by the company and has since been pursued, the proofs are full. A most experienced man of one of its constituent companies, the American Steel & Wire Company, and who had developed its foreign wire business, was given absolute charge of the development, along the lines previously advocated,

of all the export business. In 1903, the Products company, a subsidiary of the Federal Steel Company, was created for that express purpose. A systematic plan was pursued of establishing foreign distributing warehouses and of building up new freight lines and shipping facilities. It will thus appear that, whatever may be the legal consequences of the acquisition of this great volume of foreign trade, there can be no doubt of the fact that it was acquired by this company in pursuance of a well-understood purpose. The proofs also show that the diversified products of the Steel Corporation, the location of its plants for export manufacture, and its facilities generally, are the means by which this trade has been supplied and built up. And they also disclose the fact that the different subsidiary finishing companies of the Steel Corporation were, among other things, chosen and acquired by that company with a view to developing the very foreign trade, which has since been acquired. Such being the case, it logically follows that, if the possession of this great volume of foreign trade is illegal as a monopoly or restraint of trade, the Steel Corporation, of which the Products company is the mere agent, is also a violator of the Sherman Law. Was then this foreign business acquired, on the one hand, through illegal methods by the Steel Corporation monopolizing or attempting to monopolize, or to restrain foreign trade? Or was it, on the other hand, the result of lawful and fair means to expand and increase American foreign steel and iron trade without driving out those who were in such foreign steel trade, or without preventing those who wanted to enter it from doing so?

We have already seen that when the Steel Corporation entered this field there practically was no existing foreign steel trade held by American steel manufacturers. We have seen the opposition existing in such foreign markets to the building up of such trade by a newcomer; we have seen that the markets of practically all the principal nations of Europe were tariff closed to American steel, and that the spasmodic dumping policy theretofore pursued by American steel manufacturers had created a prejudice against American trade which had to be overcome.

It took the Steel Company one or two years to get the foreign

business started. It was necessary to establish and maintain a series of large warehouses all over the commercial world. Space forbids details, but the proof shows that nearly 300 places of business have been established in 60 different countries and in all parts of the world, and that great warehouses or distributing stations have been opened at strategic distributing steamship centers. Taking Belgium, for example: It was a great manufacturing country; it had a tariff and 90 per cent of its manufactured product was exported. Consequently, there was no market for the Steel Company there, except street car rails. But notwithstanding there was practically no Belgian market for foreign steel, the Steel Company located a large warehouse at Antwerp in which it stored 10,000 tons of steel products, principally pipe. It was compelled to do this, because from Antwerp it was able to reach trading centers it could not reach direct from the United States. In that regard, the proof is:

> We have shipping opportunities at Antwerp that do not exist in this country. Antwerp is a great distributing point; a large number of sailing vessels go to ports in the world that are not reached by steamers.

In the same way, while the Austrian tariff shut the Steel Corporation out of that country, it established a warehouse at Trieste, Austria, by reason of the fact that wire products and pipe can be transshipped at Trieste to ports on the Adriatic, Syria and the Mediterranean. In the same way, the Steel Company established a warehouse depot at Vancouver, British Columbia, through which it furnished light rails for lumber camps, sheet iron, wire goods and pipe. The building up of trade with British Columbia exemplifies that the steel trade acquired there was not by the Steel Company restraining or monopolizing an existing foreign trade, but was, by its creating a new and nonexistent foreign trade, in the face of serious obstacles. To reach Vancouver, the Steel Corporation was confronted by a railroad freight rate from Pittsburgh to Vancouver of $18 per ton, while the English steel manufacturer could reach Vancouver on already established lines of steamers from Liverpool to Vancouver at $7 per ton. When his steel reached Vancouver, the English manufacturer paid one third less of the

preferential Canadian tariff than the American manufacturer. The result of these adverse conditions was that, after the Steel Company opened its warehouse at Vancouver, it found that it was impossible to do much business unless the Steel Company itself established a line of its own steamers from New York to Vancouver, through the Straits of Magellan. The Products company itself, accordingly, started such a line, which is the only one from New York to Vancouver. It has four steamers of its own in service and two chartered vessels. These vessels call en route at many ports on the west coast of South America and Mexico, at some ports which have no regular steamship line. In addition to carrying the products of the Steel Corporation, they have "been carrying considerable quantities of material for other manufacturers in this country who had been unable to develop a business because of the lack of facilities." In order to obtain return freight for their steamers, the Products company has to load them at Vancouver with lumber or coal for the Gulf of California; there they reload with copper matte for Dunkirk, France; and in France they take on chalk for New York. The whole triangular trip occupies from seven to eight months and shows the hitherto unused methods and the continuous sustained effort that must be made to get and hold foreign trade. By like effort trade suited to the varied needs of various countries has been built up. Thus distributing warehouses have been established at Johannesburg, South Africa, at Sydney, Australia, in New South Wales, Copenhagen, Denmark, Barcelona, Spain, Singapore, Straits Settlements, Valparaiso, Callao, Buenos Ayres, Rio Janeiro, and other parts of the world to the number of 40. These warehouses are stocked with light rails for mines, corrugated iron for building, tin plate, wire products, pipe, and pretty nearly everything the Steel Company makes, except railroad rails. The steel for South America is carried by shiploads in chartered vessels; the Products company having under charter, when this testimony was taken in 1913, some thirty-five vessels carrying cargoes to all parts of the world. Permanent and extensive bureaus are maintained at London and at Paris, in order to sell from there to the English and French Colonial possessions, buyers for which possessions

gather at the two cities named. The necessity for sustained continuous effort is shown by the proofs. For example, the Products company has a general steel trade in the Argentine Republic of six millions a year, consisting of wire products, sheet steel, tin plate, rails, structural material, street railway material, etc. Taking the item of structural steel, the proofs show the continuous means by which such trade is obtained and held. The company located a resident engineering force there, designed and built in Buenos Ayres the first steel structural building in South America, and, as a result of the maintenance of such a permanent engineering force there, has built every steel structure in Buenos Ayres, and "we have maintained a very large office there. We are building a number of government buildings there. We built all the buildings of the Buenos Ayres Exposition. We built one for the Argentine government and one for the United States government for their exhibits there."

A similar trade of diversified articles amounting to four millions has been built up through agencies in four principal commercial centers in China, and a trade of five millions in Cuba. As evidencing that the foreign trade was largely newly created instead of taken from others, reference may be made to the trade built up in Black Sea territory. The steel sheets, pipe, and wire products from the American Sheet & Tin Plate, the American Steel & Wire, and the National Tube Companies were at first sent to Hamburg and there transshipped. The building up of that trade by the Steel Company has caused the establishment of a direct line sailing every six weeks from New York to the Mediterranean, for which the Products company furnished the nucleus of each cargo, viz., from 3,000 to 5,000 tons, but which afford shipping facilities to American manufacturers of all kinds of products. In the same way, sustained trade of six millions a year has been developed in Japan. This trade consists in pipe, railway material, structural bridge steel, light gauged steel, tin plate, and street railway material, in all to the extent of 25,000 tons per month. In addition to using the regular steamer line, three or four vessels chartered by the Steel Corporation carried out entire cargoes each month from New York to Japan of the varied products of the Carnegie Steel Company, Amer-

ican Steel & Wire, American Bridge, American Sheet & Tin Plate, National Tube, and Lorain Steel companies, respectively.

We have cited the above comparatively few foregoing proofs to illustrate the Steel Company's foreign trade, to exemplify its own continuous and indefatigable efforts to build up this trade on legitimate, commercial lines, and not by trade restraint or monopoly at the expense of its competitors. It has been the creation of a new American foreign trade, and not the monopolistic seizure of a preëxisting American foreign trade. Space constrains us to go into the extent of territory and varying character of that trade, the varied and individual requirements that had to be met in different markets, all of which show conclusively that the dumping, spasmodic foreign trade practices in vogue in the steel trade at the close of the last century were at variance with the building up of dependable foreign trade, and that with the Steel Corporation has come the substitution of reasonable, sound, and successful commercial practices in which and by which, under the proofs in this record, a dependable foreign steel trade can alone be built up. All these proofs, facts, and results serve to justify our conclusion, which we find as a fact, that this foreign trade of the Steel Corporation has not been gained by monopoly and is not a monopoly; that it does not, and has not, restrained trade; but, on the contrary, others in the steel trade have been, at the same time, free to enter such foreign trade and have done so to the extent of their resources. From a business viewpoint, the matter is well summed up by an experienced business man, produced by the government, who, speaking of the wire and nail business with which he was familiar, and of the export business of the Steel Company, says:

I would say that it is the magnificent organization of the export department of the Steel Corporation which accounts for their success to a large extent. In every country in the world they meet the conditions; for instance, they have to have different gauges in different countries and different size kegs. In Japan there is a unit there which is different from elsewhere. Ours is a keg of 100 pounds, but theirs is a keg of 133 pounds. Now, to know how to reach all the different countries and supply the needs according to the circumstances and

give them prices, and so on, in their own money, or it may be in English money, it is their wonderful organization that enables them to reach out as they do.

Q. So the organization of the United States Steel Products Company, which handles the foreign business, is a very valuable thing for the steel trade of this country, is it not?

A. Absolutely so. It is a wonderful organization.

Bearing on the systematic organization thus referred to, the proof is, in substance, as follows:

The managers of these large offices in foreign countries are almost entirely American, and nearly all of them have been trained in our offices here. We have a civil service system in our business, and our men are promoted from one office to another according to their aptitude for business in certain countries. One man might be a good business man in Brazil, and might be a total failure in Australia.

As showing that this foreign trade has been built up on business executive effort, we may here refer to the facts later noted, namely, the very material decrease in the cost of selling and the very material increase in the prices obtained. And in that connection, namely, the increase in price obtained for goods sold abroad, and the decrease of price for goods sold in the United States, the proof shows the important fact, namely, that this foreign trade has not been built up at the expense of the home market. Without entering into the details of that exhibit, it suffices to say that some 80 steel or wire products are there listed, all of which have been sold at materially higher prices in the foreign than the same articles were being sold for in the home market. We find in that list such important and widely used articles as tin plate, structural steel, blooms, billets, and slabs, axles and steel wheels, plates, bars, and hoops, T-rails, pig iron, black and galvanized pipe, seamless tubes, horseshoes, wires of all kinds, nails and spikes, fences, bale ties — for all of which higher prices were charged and obtained in the foreign market than those paid by the domestic consumer. In connection with that exhibit, we note the testimony of W. E. Corey, who says that, during the time he was president of the corporation:

The Products company had become so well established and had worked up such a line of customers and trade conditions in the world

were such that as high prices were netted to the mills on foreign business as on domestic, and on some occasions were higher on certain contracts.

It will thus be seen that the significant factor in the view of the experienced witness quoted above is in the Products company ascertaining, meeting, and supplying the individual need of individual foreign markets. And, as emphasizing his illustration of a different nail keg unit in Japan, as the basis of doing business, it might be added that to gain a foothold in the trade of India another unit was demanded, for the proofs show that in India the keg unit does not prevail at all; that there the nail unit is a seven-pound package of nails in paper packages, which are put up in such package at the nail mill at Allentown, Pa., a seaboard plant, which was acquired with the American Steel & Wire Company. In the same way the proofs show the markets of Australia demand an oval nail, while in Java a round one is required. Indeed, the absolute necessity of making different goods for the foreign markets from those made for home trade is illustrated by the proofs of the large expense necessarily incurred to meet these local foreign requirements.

A patient study of the proofs of actual business facts, difficulties, and efforts shown in the testimony of experienced business men leads us to these conclusions:

First, that the foreign business in steel and iron done by the Steel Corporation has increased from 290,000 tons in 1903 to about 2,260,000 tons in 1912, and in value from $31,000,000 in 1904 to $91,000,000 in 1913.

Second, that the Steel Corporation normally does from 80 to 90 per cent of the foreign iron and steel business of the United States; that its exports of $91,000,000 in 1913 include $30,000,000 of "reëxport" business, so called, which it does in connection with other American manufacturers using its basic products; that the "reëxport" business in connection with other companies gave employment to from 15,000 to 18,000 men, and the foreign business of the Steel Corporation to 40,000 men.

Third, that its competitors in the iron and steel business, with some few exceptions, do not seek to enter the foreign market, so long as they can get a market at home, and what foreign

steel business there was prior to 1901 had been small, and generally not profitable, and was done at from 7 per cent to 11 per cent expense on invoice.

Fourth, that the success of the Steel Company in building up this continuous foreign trade primarily consisted in its mechanical ability to make the wide range and variety of product required by foreign markets and in its manufacture of such diversified products at plants properly located for export trade. In that connection reference might be made to the proof, as showing how essential to the maintenance of foreign trade is the diversity of product which comes from broad integration:

Q. Can a manufacturer having a large line of products for sale afford to maintain such warehouses and conduct that business, when a person manufacturing only one line of goods could not afford to do it?

A. It was tried by the National Tube Company before the formation of the Steel Corporation. They established a large warehouse at Johannesburg, South Africa, and were obliged to abandon it for two reasons, one because of the cost of doing business. It cost them over 8 per cent to do the business, because they had one line of goods to sell only.

Fifth, in gradually reducing its own overhead cost of foreign selling, from about 3½ per cent in 1901 to 8 per cent in 1911.

Sixth, in gradually increasing the price of such of its product as was sold in the foreign market from 1904, when the trade had gotten under way, to 1912, while it was at the same time gradually decreasing the price of its product as was sold to consumers in the home market. These relative changes are shown by defendant's Exhibit, as follows: In 1904 the Steel Corporation sold such of its product as it exported at an average price of $27.22 per gross ton; by 1912 it was able to market them at $34.24. During the same period it was in 1904 receiving for such of its product as was sold in the home market an average of $41.44 per gross ton; by 1912 this price was reduced to $36.53.

With these facts, figures, and results proved in this record, we are warranted in holding that the foreign trade of the Steel Corporation, its mode of building it up, and its retention when built up are not contrary to the Sherman Law. To hold otherwise would be, practically and commercially, to enjoin the steel

trade of the United States from using the business methods which are necessary in order to build up and maintain a dependable business abroad, and if the Sherman Law were so construed, it would itself be a restraint of trade and unduly prejudice the public by restraining foreign trade. Happily, it is open to no such charge, for, as the Supreme Court in the Standard Oil case said: "One of the fundamental purposes of the statute is to protect, not to destroy, rights of property."

Seeing, then, the Steel Corporation, at the time this petition was filed, was engaged in the natural and normal conduct of business, both home and foreign, and that it was not then monopolizing, restraining, or attempting to monopolize or restrain, trade in iron and steel between the states or with foreign nations, we next turn to 1901, the year the corporation was formed, and address ourselves to the inquiry whether it was formed in order to so monopolize or restrain trade; or, to use the test fixed by the Supreme Court, was the Steel Company, when created, a combination which by its intent was meant to, or by the inherent nature of its contemplated acts would, "prejudice the public interests by unduly restricting competition or unduly restraining the course of trade"? Now, what is meant by the phrase "the inherent nature of its contemplated acts," which violate the statute when an illegal combination is originally formed, and which, continuing, because inherent elements warrant its dissolution whenever questioned, is illustrated by what was found to be the fact in the Standard Oil case. There the court based its right and duty to dissolve the Standard Oil Company on the two facts that: First, the Standard Oil Company destroyed the "*potentiality of competition*"; and, second, that it was "a monopolization *bringing about a perennial violation* of the second section of the act." And that there was in the Standard Oil Company of New Jersey a destruction of the power to compete — the potentiality of competition — and a perennial, continuous, and perpetual violation of the law was shown, in the court's estimate, by the following state of facts:

(*a*) Because the unification of power and control over petroleum and its products which was the inevitable result of the combining in the New Jersey corporation by the increase of its stock and the transfer

to it of the stocks of so many other corporations, aggregating so vast a capital, gives rise, in and of itself, in the absence of countervailing circumstances, to say the least, to the prima facie presumption of intent and purpose to maintain the dominancy over the oil industry, not as a result of normal methods of industrial development, but by new means of combination which were resorted to in order that greater power might be added than would otherwise have arisen had normal methods been followed, the whole with the purpose of excluding others from the trade, and thus centralizing in the combination a perpetual control of the movements of petroleum and its products in the channels of interstate commerce.

At this point we deem it proper to specially note these vitally important terms used by the Supreme Court, viz., the destruction of "the potentiality of competition," and the "perennial violation" of the statute. For, when it comes to the question of the dissolution of the combination, and that is the phase of this case we are now considering, a dissolution must be decreed whenever the inherent nature of its contemplated acts is such that from its very nature the combination was bound to destroy "the potentiality of competition," and these violations were, from its inherent nature, bound to be perennial. In other words, the Standard Oil Company had to be dissolved because its inherent nature was such that it was bound to destroy the power to compete in petroleum, and it would not be heard to say that it had no intent to destroy competition when its inherent nature had made it do so. It therefore follows that, if such destruction of the power of competition and that by perennial violation thus evidenced the original inherent illegal nature of the combination, it would seem that if a long series of years had not resulted in a combination either destroying actual competition of others, or of their power to compete, or had not resulted in the long years of the combination's business in constant, perennial violations of law, it could not reasonably be held that the inherent original nature of such combination was such as to make it unlawful when originally created and liable to dissolution whenever afterwards challenged. On the contrary, it would seem that the acts of a combination are fair tests of the real inherent nature of the combination, and that in such case the time-tried rule, " By their

fruits ye shall know them," might well serve to best gauge the source or tree from or on which the fruit matured. But, passing by this time-tried rule, with its practical tests of what the Steel Company did in the ten years subsequent to its creation, let us address ourselves to the proofs of what was done at or about the time the Steel Corporation was formed, and from these proofs alone determine whether the object of those forming it was to prejudice the public by unduly restricting competition or unduly obstructing the course of trade, or, even if there was no such intent, was the inherent nature of the Steel Corporation's contemplated acts such as to prejudice the public by unduly restricting competition or unduly obstructing the course of trade?

The iron and steel trade of the United States has been a gradual sustained evolution. So far as the metallic base is concerned, such evolution may be broadly stated to have been from iron to steel, from steel to Bessemer steel, from Bessemer to open-hearth. It is interesting to note that the next development bids fair to be from fuel smelting to electric smelting. These several stages of development have been accompanied by an abandonment and loss of equipment of great value, and have necessitated vast further expenditures for new appliances to make the new open-hearth steel product. To illustrate, referring to a single one of the rapid revolutions in steel making—the removal of phosphorus in pig iron in the Bessemer or open-hearth processes by the substitution in the lining of lime for a silicon base. This single chemical fact, made public in 1885, "practically revolutionized the iron industry, and by the year 1890 basic open-hearth steel had practically supplanted the use of wrought iron for all commercial purposes." Side by side with these rapid metallurgical changes of product there was at the same time going on radical changes in the mechanical handling of the product. To refer to but one of the many mechanical changes, "in the late 80's the introduction of electricity as a motive power also produced another revolution in the steel industry, so that practically all works had to be rebuilt if they desired to keep abreast of the recent developments of the art." But not only were metallurgical and mechanical changes taking place with regard to the different stages of metal production,

but there developed at the same time a radical change, not of one product or one stage, but of all stages in the way of rounding up plants, or, as it is called, integration, so that continuous processes could be carried on. In the old method of wrought iron making there was no continuity of operation. The molten metal produced by a blast furnace was run into pig iron. This pig iron was transported to a rolling mill, where it was first puddled, and then rolled into muck bar, which was again suffered to cool. The muck bar was again heated and rolled in finishing mills. As steel making progressed, its manufacture by various agencies not necessary here to detail, became a continuous fluid process. Instead of the metal being suffered to cool, it was continuously treated first as a fluid, and then as an ingot, but always without entirely losing its initial heat. But these steel plants, with their continuous processes and their increased capacity to produce, serve to confront the finishing plants with grave problems in reference to their basic supplies. This era of change and its new problems is testified to by Percival Roberts, Jr., whose experience and relation to the steel business give weight to his summary of the changing conditions and problems confronting that industry. He testified:

I think I had reached the situation existing as of the late 80's when basic open-hearth steel was gradually, or rapidly, I might say, supplanting wrought iron. The wrought iron plants that were of smaller capacity and had insufficient capital or lack of sufficient tonnage to dispose of the product of an economical steel plant commenced purchasing billets and blooms from those who had converted their plants into steel-manufacturing ones. This production of billets and blooms was practically a by-product with the finishing mills. In times of activity they had very little surplus product to spare. When not so pushed on finished material, they disposed of part of their steel-melting capacity in the shape of semifinished material. The iron plants purchasing this material found that the same could not be carried on successfully, due to the fact that it required an almost unlimited capital to be locked up in supplies of billets, as finished material required so many different weights of billets and blooms that the stock on hand had to be enormously large; also the chemical requirements of orders requires that different grades of steel should be used. This also required a vast amount of material to be carried at all times on hand.

Another matter which occurred about that time changed very materially the situation, and that was the introduction of what was known as the Jones mixer. I might say that up to that time the production of all blast furnaces was run out from the furnace in the shape of liquid pig iron, and cast in the sand and allowed to become cool. The invention of the Jones mixer was for the purpose of carrying on the production of steel as one continuous operation from ore to the finished product, never permitting the material to become cold until it reached the final economic shape. I do not mean to say that this applies to all finished shapes, but to a cross section of material at which it would be economical to let the material cool.

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The Jones mixer is a large vessel placed between the blast furnace and the steel works in which the product of the blast furnace is run in liquid form, making a large reservoir of fluid pig iron from which ladles are taken in liquid condition the contents in liquid condition and used in Bessemer converters or open-hearth furnaces. The advantage of this process was that it reduced the cost of manufacture in this one respect alone by about $1 a ton, which is the cost of remelting cold pig iron for steel production.

The situation from 1890 on grew more and more acute. Those concerns which had become more or less integrated and had changed their methods from those of iron to steel were continuing their integration to even a greater extent than before, although I would like to say that even prior to the introduction of steel the matter of integration was one of varying degree, even in the manufacture of wrought iron, although there was not the same necessity for it. In those days one man mined ore; another man ran a blast furnace; another man operated rolling mills. The processes were all disconnected.

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Coal and limestone were sometimes separate, sometimes controlled by one party, but even in those days there were certain establishments which controlled their material from the ore and limestone up to the finished wrought iron product, so that even in those days iron manufactures were not on the same basis as regards competition. Those concerns whose output — I speak now as of about the year 1890 — those concerns whose output was of a character and of sufficient tonnage, and who controlled sufficient capital to enable them to convert their works from iron to steel, did so, but there were a vast number of those whose character of product was of a less heavy nature, such as sheets, small bars, light plates, etc., who neither had the capital nor

the output to warrant them in making, or rendered it possible for them to make, this change. There was also another class of establishments, namely, the blast furnaces who had heretofore supplied the puddling furnaces or the rolling mills with their pig iron for making bars. Those concerns found themselves without customers and they in turn were forced to develop a product which would take the place of their former ones. These smaller concerns were buying, as I say, to the best of their ability, their billets, blooms, and slabs from the larger concerns, who were making them in a certain sense as a by-product during the years from about 1890 to 1896.

These revolutions which I have spoken of, due to the introduction of basic, open-hearth steel in place of wrought iron, were the fundamental reasons for all the earlier aggregations of work which took place about the year 1898, and through that year down to, say, 1900. Certain of them were integrated like the Federal Steel and the Carnegie Steel Company backward to their supplies of raw material, and to the extent which they had formerly been consumers, they to that extent became producers. The other concerns, like the National Steel, were composed largely of blast furnaces that had lost their custom for pig iron, and who found themselves compelled to produce, instead of pig iron, billets and blooms for sale to those who had formerly used wrought iron. The Tin Plate, the Sheet Steel, the Hoop, the American Steel & Wire were composed of concerns who individually were neither able, for want of capital or amount of output, to change from wrought iron or to manufacture steel in sufficient quantities to make it commercially profitable to do so.

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The Tin Plate Company had been a consumer, and not a producer, of wrought iron product, and, in fact, the manufacture of tin plate had not taken place in this country until after the introduction of the use of open-hearth steel. So far as I included them in my answer, I meant to state that they individually were unable to produce the raw material from which their finished product was made, but by combining these individual units they would be enabled to do so economically.

The tendency of the steel business during these years towards concentration, combination, rounding up, or continuity of operation is reflected in the census figures. On the one hand is unprecedented growth in the volume of the steel and iron business done and of the increase of capital; on the other hand is a striking decrease in the number of establishments doing it. Thus Bulletin No. 78, Census of Manufacturers, 1905, says:

The growth of steel production has been the heaviest of any portion of the iron and steel industry. The product for 1900 shows a gain over that of 1890 of 6,510,348 tons, or 155.9 %, or an average increase of about 650,000 tons per year. The product of 1890 shows a gain over that of 1880 of 3,147,271 tons, or 306.3 %, an average increase of nearly 315,000 tons.

Whether the cause of this enormous increase of production on the one hand was due to the rounding up process, of decreasing the number of plants, and further expanding those that remained, the bulletin in question is, of course, speculative, but does show that decrease in the number of corporate plants with increase of capital in those remaining was the actual fact in the iron and steel business. In that regard the same bulletin showed that there were in 1880 in the United States substantially 1,000 of such establishments with a capital of $230,000,000. By 1890 these 1,000 had decreased to 838, but the capital of those that remained was increased to $425,000,000. By 1900 the 1,000 establishments of 1880 had again decreased to 763, but the capital of those that remained had grown to over $600,000,000. During the same period the separate blast furnace establishments had also decreased. In 1880 they were 483; in 1890, 377; and in 1900, 273. This census evidence of widespread general change, readjustment, and concentration by practical men in the iron and steel business would seem necessarily to have had some impelling cause — economic, mechanical, metallurgical, or administrative — back of it. And, in the absence of proof to the contrary, the conclusion of Mr. Roberts would seem reasonable that "these revolutions which I have spoken of, due to the introduction of basic, open-hearth steel in place of wrought iron, were the fundamental reasons for the earlier aggregation of works which took place about the year 1898, and through that year down to say 1900," and that the business reasons which induced practical steel men to so act was the fact that, unless they did so, the changed conditions of the steel business might force them out of business.

This testimony serves to show how radical, extensive, and enforced was the steel integration, which, summed up in a few terse words of this business man, really meant a rounding up

and readjusting of everything, as the witness says, "from the mining of the ore to putting on the market of the finished product," and an increase in that company's case of resources from $600,000 to over $23,000,000. From these figures the insistent necessity of integration in the steel business will be seen.

Coincident with these mechanical and metallurgical changes another basic change of peculiar and dominating importance in the steel business was also taking place. This was in freight and transportation. This change, it will be seen, not only restricted the range of a plant's market, but by doing so necessitated what might be termed locality integration. The chief factor in the manufacture of steel is labor, and the next is the locality where it is produced; being of great bulk, the transportation of the raw material to where it is made and the freight to where it is used are the factors decisive of its being profitably made and sold. As illustrative of the vital character of freight as a factor, the proof is that the Steel Corporation uses 45,000 tons of ore alone a day, not to mention coke or limestone. The delivery of the steel to the user, and the net gain over cost received from him, is, of course, the practical test of steel making. From these self-evident business truisms, it follows that the tonnage of bulky steel products restricts its steady, natural, and sustaining market to the consumption of the territory near its place of production; for example, great as is the consumption of steel in the New York district, and ample as is the productive capacity of the United States Steel Corporation to supply it, yet the proof is that the Steel Corporation does "very little business here (New York) compared with that done by the mills in Bethlehem, Phœnixville, and mills located near here." Prior to the regulation of freight rates by the government through the Interstate Commerce Commission, freight stability was unknown. Special rates to large shippers, cuts in freight rates, and secret rebates were common practices between the steel producers and the railroads, and these enabled steel manufacturers to ship bulky products into territory naturally supplied by other manufacturers, and by these cuts, special rates, or rebates to dump their surplus product in districts which they could not enter if they paid proper freight charges.

When, however, under the regulating power of the government, freight stability was enforced, the steel maker's market was at once locally restricted, and his only way of overcoming the regular, stable, adverse freight rate was to integrate locally; that is, to erect or acquire other mills in the market locality from which freight forbade his heavy product entering. The embargo laid by freight on distant markets is simply a business fact, and it suffices to say that, while the government by this enforced transition of the steel shipper from the era of unstable freight cuts and rebates to an era of freight stability in the end contributed to corresponding benefit and stability in the steel maker's business, yet it must not be overlooked that, in thus narrowing his market, the steel maker was compelled to broaden his market by expanding his operations so as to manufacture in additional localities. Coincident with this tendency to integration and to the consequent widening of variety of product and to the entry of steel into new fields, a radical change in the variety of ore supply was necessitated. In thinking of iron ore, we are apt to regard it as simply ore, and overlook the fact that there is a radical difference in different ores. In the earlier manufacture of iron, practically any ore could be used, but as the steel era came along with its chemical tests, and the specified requirements incident to its use in varieties of articles, the particular character of the ore base became more and more a matter of importance. The practical proof of this wide range of various ores required is illustrated in the proofs, which is that, even with the wide range of ores owned by the Steel Company, it is at times unable to meet the requirements of purchasers.

We noted above where 18 different kinds of billets were required in a wire mill alone. The proof is that it is only by a scientific mixture of different sorts of ores that steel of the large range of specified steel requirements can be made. This simple statement of a few lines, when carried into practical business operations, means the furnishing of many varieties of ores that may be as far away from a blast furnace as Minnesota, Chili, or Cuba. These must be bought, mined, transported, fluxed, and treated in order to meet, for example, the exacting structural requirements of a steel rail. To successfully produce that rail in

great tonnage, which, under the proofs, is a business necessity, every step in that long spread from the ore in the ground to the finished rail must be under the integrated control of that agency which is ultimately held responsible by the railroad for the rail.

The result of these radical and forced changes in steel making evidenced itself in the rapid and widespread fever of integration by consolidation that took place toward the close of the century. Whether, from such consolidations, monopoly, rise in prices, and restraints of trade were hoped by many of their promoters to be obtained, it is certain that the deep-lying motive which led practical steel men to put their plants into such consolidation was the recognition of the absolute business necessity of integration as a condition of staying in the steel business. Thus the Carnegie Steel Company, occupying, as it did, the commanding position in the steel trade, varied, as were its products, having fully 70 per cent of what foreign trade there was, and having the foremost place in the home markets, itself felt the necessity of and was preparing to enter on further integration by widening the variety of its product. While leading in some lines, it was deficient in others, notably pipe and wire, which consumed much of its basic products.

So also had the Carnegie Company determined to integrate by adding the important items of pipes to its finished product. The purpose of this was to create for itself and in itself a customer that would use part of its product by making it into pipe. This item of steel consumption, embracing oil, gas, water, irrigation, and kindred fields, the Carnegie Company, as we have seen, did not make. That this vast field of basic steel consumption was not sufficiently filled is shown by the fact that they planned to spend in additions for such pipe making mills, excluding land, $12,000,000. The plans for this enterprise were entered upon in 1897 or 1898. It will also be seen, in discussing later the acquisition by the Steel Corporation of the Seamless Tube Company, that the Carnegie people were carrying on substantial experimental work at the Seamless Company's plant with a view to itself entering the tube field. Efforts had been made to get a site near Pittsburgh, but sufficient acreage for the large works in view could not be found. Meanwhile, a site of

5,000 acres was secured at Conneaut, on Lake Erie, where the company's ore steamers coming from Lake Superior delivered the ore to the company's railroad for transit to Pittsburgh. From this point, water transportation for pipe was available to seaboard and to the entire territory tributary to the Great Lakes. The testimony is that this proposed widening of the Carnegie Steel Company's product variety to include pipe and wire products was absolutely "in good faith as indicative of the intention and purposes of the Carnegie Steel Company."

As evidencing not only that fact, but that it was a necessary and far-sighted integration (one called for by the legitimate future of the business), will appear from the fact that, after the Steel Company was formed and its comprehensive plan of complete integration was carried out, that company expended $13,000,000 in building the pipe plant which the Carnegie company in 1900 planned to build, and it will be noted further that it built it in the immediate Pittsburgh district, on ground near the National Tube Works, where the Carnegie company was not able to get the required site. All of which seems to strengthen and confirm the conclusion of the insistent requirement of integration in the steel trade at the close of the century. The like compulsory integrating influence thus shown in the Pittsburgh district evidenced itself also in the great Chicago steel district. In that district the Illinois Steel Company held the same commanding local position as the Carnegie company in the Pittsburgh. Its natural market was the Chicago district. It had a rail market in Canada at times which could not be reached by the Carnegie. In spite of the allegations of foreign trade made by its then management, it really had little or none and really could have no profitable foreign trade. Such foreign trade as it had to Canada was of the spasmodic character heretofore referred to. It had large plants at Chicago and Joliet, Ill., and at Milwaukee, and had railroad properties, but its product of basic open-hearth steel was, even in 1890, only 190,000 tons, as compared with the Carnegie Company's 1,250,000 tons. It lacked the finishing units of sheet steel, steel hoop, and tin plate mills, that were afterwards acquired in pursuance of the integrating policy which the plans of the United States Steel

Corporation contemplated. Practically it had no substantial wire or structural output and no tube or pipe output at all. In 1898 the Illinois Steel Company entered on an effort to integrate by consolidation and with foreign trade in view. In pursuance of its integrating policy, the Illinois company formed the Federal Steel Company, which took over the Minnesota Iron Company. This gave the Federal a Lake Superior ore reserve, its own railroad transportation to Lake Superior, its ore fleets to Chicago and lake ports. It also took over the Lorain Steel Company, which gave it mills in the Cleveland district, and at Johnstown, Pa., in the Pittsburgh district, and a relative approach to the seaboard. These mills were then regarded as enabling the Federal company to supply foreign trade from those districts. This expectation was to that extent justified, for the proofs show that, so far as their individual products are concerned, the Lorain and Johnstown mills are now very substantial factors in the foreign trade developed by the Products company. But apart from these mills the Federal Steel had no facilities for entering into foreign trade, and the proof is that, even with all the facilities for entering such trade possessed by the Steel Company, but 2 per cent of the product of the Illinois Steel Company now goes into foreign trade, and that part goes, not into such general trade, but only into such Canadian markets as its location permits. The integrating steps thus mapped out are recited in the proofs, but these partial efforts at complete integration proved disappointing in that it was not complete enough.

Realizing these limitations, and that the Federal Steel Company's operations were not rounded to a successful manufacturing future, the proofs show that steps had been taken just before the United States Steel Corporation was formed to raise from $40,000,000 to $45,000,000 in further integrating the Federal company. That such steps by the Federal company had as their real basis the bona fide commercial and industrial requirement of further integration is, just as we have shown in the case of the Carnegie Steel Company, also shown in the Federal's case by after events in connection with later events in the Chicago district. The record shows that the Federal com-

pany was not equipped to make pipe and sheets at all, and plates only to a relatively small extent, and had no complete line of finishing mills. It further shows it lacked adequate open-hearth capacity, did not have the money to extend it, had very limited structural product facilities, and even with its ore supplies it had to buy other ores to get the proper mixtures. After the Steel Company was formed, in order to supply the needed rounding-up equipment of the Chicago district, which the Federal lacked, the Steel Corporation made large additions in that district at Gary, in the center, and at Duluth on the northern limit, with a view to reaching from Duluth the western Canadian market. In that regard the proofs show that some $80,000,000 were spent in building at Gary open-hearth plants, a rail mill, structural steel plants, bar mills, sheet mills, and plants of the American Bridge Company and the American Sheet & Tin Plate Company, in all of which facilities the Illinois and Federal companies were deficient. Along the same line the proofs show that $10,000,000 are being expended at Duluth to erect blast furnaces, open-hearth furnaces, and bar and merchant mills with which to supply the American and Canadian Northwest. As evidencing this trend to further integration, the desirability of the Federal Steel Company acquiring the Carnegie company and thus integrating eastward was, in 1899, brought to the attention of the Federal Steel Company by a representative of the Carnegie Steel Company, who then suggested:

That it would be a good thing for the Federal Steel interests to purchase the Carnegie property and perhaps with them some other properties, which included finishing mills of various kinds, suggesting companies, the Wire Company, the Tin Plate Company, and some other companies.

The matter was actively taken up by the Federal company, but eventually fell through, because " Mr. Frick was not willing to agree that the whole Carnegie organization, including himself, would remain in the company and assist in carrying on the business." The proofs further show that early in 1900 Mr. Schwab, the president of the Carnegie company, urged the buying of

that company by the Federal, and efforts were again made to have Mr. Morgan, who was a member of the board of the Federal Steel Company, take it up, which he declined to do.

This demand for integration which thus evidenced itself in these two leading companies, each attempting to integrate back to the base of supply and also into more extended and diversified finished product, also evidenced itself in other branches of the steel trade. This was the integration of mills which were large consumers of plates, ingots, billets, sheets, rods, structural iron, and other semibasic products. Without specifying all, we may refer to the steady integration of these various subdivisions of the steel trade. This began in December, 1898, when the principal tin plate manufactories integrated by consolidation into the American Tin Plate Company. In January, 1899, the American Steel & Wire was formed by a consolidation of all the leading wire product manufacturers. This was followed in February, 1899, by the consolidation into the National Steel Company of 12 per cent of the ingot production of the country, which was located on the eastern side of Chicago and the western side of the Pittsburgh district. The same month saw the National Tube Company formed by great concerns making various kinds of tubes and pipes. In March of the same year, sheet steelmakers in large tonnage combined to form the American Sheet Steel Company, and in April of the same year, the American Steel Hoop Company was formed by the leading makers of hoops, bands, and cotton ties. While the American Sheet, the American Hoop, and the National Steel were separate companies, yet for integrated, continuous working, they were in effect necessary to each other.

This integrated relation is no doubt the manufacturing feature on which it was insisted that the finishing companies would not sell to the Steel Corporation unless the National was also purchased, as Mr. Carnegie insisted should be done. In the same month we find the principal structural and bridge erectors and producers forming the American Bridge Company. In connection with this consolidating and integration of structural manufacturers and fabricators, it is but just to note, as illustrative of compelling forces outside that industry, the demands which the

business world was making upon the structural steel industry. Thus in referring to the American Bridge Company, and its carrying forward at a later date this policy of expansion and local integrating of its works, the proofs show that such great operations as the tall buildings of recent origin, such railroad work as the Hell Gate Bridge, and such national work as the Panama Canal, practically necessitate the existence of such companies. In that respect the proof is railroad bridges are —

> confined to those companies having the largest plants and those equipped for that sort of work. There are very few companies, for example, that could build a bridge like the Hell Gate Bridge, involving 40,000 tons of material and an incidental expense of perhaps $300,000 to get the falsework together. When we secured that contract we had to expend immediately $160,000 for tools. While we were a very large concern and had a very well-equipped plant, we were obliged to buy $160,000 worth of tools for that particular work. . . .

The proofs also show it is necessary to have structural plants in different localities.

They further show that it requires a large plant to deliver such contract requirements so as to coördinate with other parts of the work.

It will thus be seen that these large modern operations practically necessitate correspondingly large manufacturing facilities and financial resources to adequately and successfully meet such product demands. These rapid, widespread, and isolated integrations of different subdivisions of the steel trade cannot be reasonably explained on the sole theory of a widespread, dominating purpose in each of these aggregations to monopolize or restrain trade. In the first place, the proof is simply one-sided that they did not control trade, and that in spite of their size and large proportions of then existing trade, their competitors, as we have already seen, have increased more rapidly than they. So that, while there may have been in the minds of those who formed them the possibility of monopoly and increase of price, we are inclined, from a study of the proofs in this case, to the belief that the real underlying influence was the economy of management, the locality of production and market, and the

continuity of process which resulted from such integration. Take, for example, the last one formed, the American Bridge Company. During the years it has been a subsidiary of the United States Steel Corporation its business has increased 42 per cent. In that time, its competitors have increased their business 164 per cent. During that time the American Company has had the help of all the associated subsidiary companies of the Steel Company, it has shared in all the economies of management, coöperation and financial help rendered by the parent company, yet with all these aids, its competitors have increased their business four times as fast as its own. It would seem, therefore, that the American Bridge Company had even less hope or power to monopolize when it was originally formed and stood alone, when it could not, when bought by the Steel Corporation, so monopolize the steel structural business of the country. In view of such facts, we have been impressed with the view that these consolidations and integrations, accomplished or in view at the close of 1900, were more largely made with a view to meeting the changing conditions in the steel trade in its transition from iron to steel and in its adjusting itself to the progress, improvement, and development in that industry rather than with monopolistic intent. The proof in regard to the reasons for the formation of the American Bridge Company fairly states, as it seems to us, the basic reasons which led to the unifying of the separate branches of the steel industry. Thus, it is testified, with respect to that company's formation, as follows:

A. The purpose of the formation of the American Bridge Company was simply along the lines of economical shop management, and had no reference whatever to any monopoly or to securing the entire industry of the country. The plants which became a part of the American Bridge Company were believed to be in a position to be operated more economically as a combined whole than as independent units, and the foundation of that company was the securing of a steelworks whereby they could obtain, to a large extent, the control of their raw material for fabrication, the basis of practically all structural contracts being one of time; the time of delivery being the most important factor in practically 90 per cent of all contracts taken. These independent units found themselves at that time in a very disadvantageous

position, due to the fact that the large steel plants were commencing to do their own fabricating, whereby they were enabled to control their rolling mill supplies and make such deliveries as these independent fabricating shops, having no control over the raw material, could not do.

There was also another reason for it, namely, that contracts were increasing so rapidly in magnitude that as independent units they were unable to secure sufficient working capital to enable them to fabricate these large tonnages.

You can trace from the very beginning of the securing and assembling of their raw material through the designing, fabrication, transportation, and erection work, and the increase in their working capital, the reasons for putting together those plants, which were of two principal characters: First, they were partly competitive, I might say, by reason of a greater or less similarity of output and by reason of a common territory into which the transportation rates enabled them to ship the material; and, second, plants absolutely non-competitive, due, (a) by reason of an entirely dissimilar output, and (b) by reason of their geographical location.

The whole scheme was one to decrease cost of production and to operate along the lines of what, at the present time, is termed "scientific shop management." As a matter of fact, any advance in prices was not discussed to my knowledge; nor did any such enhancement ever take place. Competition at all times was extremely severe, and the profit on the output decreased from the time of the formation of that company until the present day. A number of concerns were offered to the American Bridge Company at the time of its formation, which were declined for various reasons, because they did not seem to be essential in the rounding out of the proposition that I have referred to.

As we have said above, it may have been the fact that, apart from the operative necessity that led to many manufacturers putting their works into these consolidations, there was probably a purpose also to monopolize and restrain trade, yet by the time the Steel Corporation was formed the inability of these prior combinations to so monopolize trade was proven to those who gave heed to facts and figures. Indeed, as we gather the net results of these different plants in varied steel lines, the acquisition of which (1901) by the Steel Corporation is alleged to evidence a purpose to monopolize, the facts and figures show that in only one product, namely, that of ingots and castings, had there been an increase of proportion in the three preceding years

by these plants, and in nine other branches, the plants which the Steel Company subsequently acquired had in point of fact in those three years clearly shown their inability to monopolize by a decrease of relative percentage ranging from 1 per cent in the case of plates and sheets to 16 per cent in wire nails. And that this three years' decrease in actual monopolistic control was the normal trend of the steel business is shown by the fact that such proportions continued to decrease after the Steel Corporation was formed. As an example of this tendency we may cite the wire plants subsequently acquired by the Steel Corporation, which in 1898 had 88 per cent of the country's production and in 1890 had fallen to 72 per cent, had by 1911 so continued to lessen their proportion of the part sold in the American market that it was then but 42 per cent of the country's production.

We have thus seen the unifying, integrating, and rounding-up influences which were irresistibly forcing those engaged in the practical work of making steel to form these prior combinations of integrating units. The proofs show that Mr. Morgan was a director in the Federal Steel Company, but that he personally knew nothing of the steel business. His firm had taken part in some of these consolidations, but the suggestion of the absorption by the Federal of the Carnegie company had not appealed to him. The proof is that while he was a member of the board of directors of the Federal Steel Company and was financially interested in it, he had probably never attended a meeting of the board and taken no part in its management and knew nothing of the practical steel business. The conditions in the steel trade being such as we have shown above, Mr. Morgan, in December, 1900, attended a dinner in New York where some 80 men, prominent in steel manufacturing and the banking business, were present. This dinner was given to Mr. Schwab, the president of the Carnegie Steel Company. Whether the dinner was given for the purpose of affording an opportunity of interesting Mr. Morgan in buying the Carnegie Steel Company, which the bitter differences between the partners in that company and the desire of Mr. Carnegie to retire from business then made possible, there can be no doubt, in view of the outcome, that Mr. Schwab then gave to the bankers present, and

particularly to Mr. Morgan, who was seated beside him, such a comprehensive view of the steel trade as was well calculated to show the possibility of carrying integration to its logical manufacturing and merchandising efficiency, and afforded the Federal company, of which Mr. Morgan was a director, the opportunity to carry out, on a large scale, the policy of integration that company had planned and had attempted to carry out. And there can be no doubt that Mr. Schwab realized that if a sale of the Carnegie company could be made the grave discord among the partners of the Carnegie company which had arisen, could be ended, and the policy of integration on which, as noted, that company had also embarked, could be carried out by some larger organization. Indeed, the evidence is clear that there was an earnest desire on the part of the owners of the Carnegie company for several reasons to sell.

With these matters no doubt in view, Mr. Schwab made an address as already quoted, and brought into clear relief three propositions: First, that steel making had then reached the limit of improvement in metallurgical methods; second, that further advance was dependent on integrating processes; and, third, that to take care of the growing steel production a great foreign trade was possible. It is suggested that this whole talk of integration or rounding up of manufacturing facilities is an afterthought, and a mere cloak to veil a concealed purpose to monopolize trade. Let us examine what the proofs show in that regard.

Looking only at the two great companies, the union of which made possible the steel company, the Federal and the Carnegie, we have the fact that both these companies had been themselves gradual integration growths, and their managements were then trying to integrate them further. The Illinois Steel had entered into the wider field of the Federal; it had integrated back to ore; it was trying to integrate locally into eastern markets through Lorain and Johnstown, had considered the acquisition of the Carnegie company and had planned to spend some forty to fifty millions of dollars in further broadening its field of products. For making the great basic products of open-hearth steel, which was then becoming the dominant factor in

steel, the proofs show the Federal was not equipped. The subsequent location of the great open-hearth plant at Gary alone shows the existence of the Federal's prior need of further integration without reference to the fact that it was lacking in finishing mills for rails, bars, structural, sheets, etc. In the same way we have seen the Carnegie company was lacking in finishing plants for tubes, wire, hoops, and many other finishing plants to use its sub-basic product. These patent facts and urgent needs — facts which, as we have seen, were set forth at the time in the minutes, letters, and communications heretofore quoted — evidence the existence of the practical manufacturing necessity of both these two great companies, either building or buying finishing mills. That such purpose of manufacturing integration should have been elaborated and formally set forth as the reason for its purchase by the Federal company of the Carnegie company would not, in the nature of things, be done. Every one concerned knew these facts without their being stated. It was a thing every steel man recognized so fully that no specific reference would be naturally made to it. But the proofs do show that, whatever purpose was in the minds of those forming the Steel Company, integration was certainly one of the special objects in view. Thus, Mr. Schwab makes it clear that "the economic advantages to be derived" were more enlarged upon even than foreign trade. "I might say," is his testimony, "that I enlarged, and perhaps made a more strenuous talk to Mr. Morgan, upon the subject of export and our ability to export, and foreign business in foreign markets, than any other excepting only the economic advantages to be derived."

It will thus be seen that here was a complete outline of a manufacturing plan which, if carried out, enabled the Federal company to integrate from or to varied finished products, and this not only in the Chicago district, but, through the acquisition of the Carnegie company, through the Pittsburgh district as well, and through this latter district to reach the foreign markets, which it was powerless to reach from its own district, and through acquisition of the finishing mills held by the Tube, the Sheet, the Wire, and Bridge companies to obtain the varied product facilities by which alone successful foreign trade could

be built up. The testimony of Robert Bacon also shows that the whole plan turned on the possibility and advisability of the Federal buying the Carnegie company, and, if that could be effected, that certain other units should be bought to provide adequate finishing plants.

These proofs certainly tend to show that the practical manufacturing question of rounding out or integrating the Federal company by acquiring finishing companies was one of the objects its directors had in view at this meeting. The proofs also show that these several finishing mills were consumers of such basic products as were made by the Federal and the Carnegie, and that those two companies had no such finishing mills of their own as was adequate to consume the product they made, which was suitable for such mill. Without entering into the details of the proof bearing on these several finishing companies, all of which, together with the comments thereon are to be found in the Statement of the Case, page 63 and following, we may say that they fairly show that without the acquisition of each of the finishing companies named, viz. the American Steel & Wire, the National Tube, the American Bridge, the American Steel Hoop, and the American Sheet Steel, the Federal Steel Company, even with the acquisition of the Carnegie, would not have been provided with adequate finishing facilities for consuming its sub-basic product. And further, without acquisition of the first three, the Federal would lack several of the most important products that have entered into the foreign trade built up by the United States Steel Products Company. It will also be noted that, in addition to the affirmative testimony quoted above tending to show that integration along manufacturing lines and development of foreign trade were among the avowed purposes of those who formed the Steel Corporation, there is a negative testimony of those who took part in forming the Steel Corporation, and quoted below, that monopoly of the steel and iron business was not the purpose for which that corporation was formed.

First. That with the competition left outside of the Steel Company, the extent of which has already been shown, a monopoly of the steel and iron business of the United States was simply

impossible, and that no effort was made to secure these companies.

Second. That in view of the fact that the proportionate volume of competitive business has increased since the Steel Company was formed and that the proofs show no attempt by it to monopolize it to the exclusion of its competitors, to now attribute to those who formed the corporation an intended monopolization would be to say that, having formed the corporation for the purpose of monopoly, they immediately abandoned such purpose and made no effort to accomplish it.

Third. That the publicity, which the proofs show the Steel Company has from time to time made its prices, its accounts, and its policies, would seem a practice in line with legitimate business, rather than with illegal monopolization.

Fourth. That in carrying out the plan the advice of Abraham S. Hewitt was taken by Mr. Morgan, and at the latter's request Mr. Hewitt went on the board and served until his death, is a fact which, in view of the high character of Abraham S. Hewitt, tends to negative the contention that the purpose in view was to violate the law.

And lastly, as stated above, there is affirmative testimony that no such object was in view. In that regard the testimony of Robert Bacon is not to be overlooked. His service as Secretary of State under one administration, as Minister to France under another, coupled with the selection on his retirement from business to positions of educational character, warrant this court in attributing weight to his testimony. The testimony of Judge James H. Reed, of Judge Gary, and of Charles M. Schwab is to the same effect. Recurring, therefore, to the particular question with which this particular part of his opinion deals, namely, whether we should now enter a decree dissolving the Steel Corporation on the ground of its inherent illegal character in 1901, and whether we should also dissolve the several constituent companies which it acquired on the like ground of their original inherent illegal character when they were formed, we think there is ground for our holding, in view of the facts, proofs, and views above set forth, that we are not, as a court of equity, warranted in taking such a drastic course as to now decree

the dissolution of the Steel Corporation or its constituent companies.

We are, however, pointed to the subsequent acquisition by the Steel Company of several properties as being attempted monopoly or restraint of trade, and as evidencing an original purpose to monopolize and restrain. The first of such was in August, 1901, when the Steel Company bought the Shelby Steel Tube Company. Whatever may have been its motive at the outset, it is clear the purchase effected neither monopoly nor restraint of trade, for we have already seen that while, even with the acquisition of this company, the Steel Company's output of seamless tube, during the ten years of its existence, has doubled, during the same period its competitors' sales have grown sevenfold. In the light of such figures and facts, we are of opinion that the acquisition was simply in the due course of normal business, and, indeed, was but the virtual carrying out of integration plans of the Carnegie Steel Company that long antedated the formation of the Steel Company. Without entering into minor details, we may say that no proof of monopoly or trade restraint was shown beyond the conceded fact of purchase, and the fact that the new article of seamless tubing was in some uses supplanting lap-weld. The old type of tubing was called "lap-weld" and made by the National Tube Company. The Shelby company made a different article, called "seamless" tube. While in some ways lap-weld and seamless were in competition, yet their main uses were not the same. The Shelby Company held a basic patent involving the piercing, at an early stage, of the billet from which the seamless tube was drawn. Before the purchase of the Carnegie Steel Company by the United States Steel Corporation, the former company, in pursuance of its purpose to enter the pipe business, was carrying on some experimental work in seamless tube making at the Shelby Company's plants, and its management had become convinced that the Shelby method was the proper one. Meanwhile the National company had also determined to enter the seamless tube field, and to that end had bought the Standard company. The latter made seamless tube under a patent granted to two former employees of the Shelby company. Its business

in the seamless tubes was very small, and it had previously tried to consolidate with the Shelby company. Much patent litigation had resulted; the National company carrying on the contest for the Standard company.

When the Steel Company was formed, two divergent views were thus presented by the managements of two of its units. The National Tube, represented by Mr. Converse, contended the Standard's process and machinery was the proper mode of seamless tube making. The Carnegie Company, represented by its president, contended the Shelby method was the proper one. The determination of the matter seems to have been made by two directors of the Steel Company who had taken no part in the contest between the National Tube Company and the Carnegie Steel Company. Their testimony is that they became convinced that the patent of the Shelby company controlled the situation. That company would only sell its patent, however, if the Steel Company also bought its plant. Such purchase the Steel Company made in order to get the patent. In view of the fact that the Shelby patent has been sustained by the courts, that the Steel Company on its purchase abandoned the machinery used by the Standard company, and has since manufactured under the Shelby process, we are satisfied that the acquisition of that company was an ordinary purchase, and had no other purpose than to acquire and use the legal monopoly which the Shelby company had obtained from the government by its patent. And a purpose to restrain and monopolize the pipe business is negatived by the fact that no monopoly has resulted and that pipe sells for $20 a ton less than when the Steel Company was formed.

The next matter in the line of alleged monopoly and trade restraint was the purchase by the Steel Corporation of the Union Steel Company in December, 1902.

We are of opinion that the purchase of the Union company was a natural and normal acquisition, incident to the growth, increase, and needs of the Steel Corporation's business, and was not done with a view to monopolizing the steel business, or to restrain trade by eliminating competition.

We next turn to the acquisition in May, 1904, of the Clairton

Steel Company. The Crucible Steel Company was engaged in the manufacture of tool and finer grades of steel, which the Steel Corporation did not make.

The next of these acquisitions by the Steel Company, which it is alleged was made to monopolize or restrain trade, is known as the Great Northern ore lease, which was a lease on royalty of some thirty-nine thousand acres of Lake Superior ore lands in August, 1907. This lease provided for the payment of a minimum royalty of 750,000 tons to be mined in 1907, 1,500,000 tons in 1908, and an increase of 750,000 tons each year until 8,250,000 tons was reached in 1917. That yearly amount was then to be taken out until the lease ended in 50 years. The royalty was, using round figures, $1.17 per ton on 49 per cent ore, $1.21 on 50 per cent, and $1.98 on 66 per cent ore, with an increase of 3.4 cents per each year on all grades. The lease provided the Steel Company had the option to cancel it as of January 1, 1915. During that time the lessee had full rights to test the premises. In pursuance of such right of cancellation, the Steel Corporation early in 1911, and prior to the filing of this petition, gave notice of cancellation, in pursuance of which the lease was subsequently surrendered. It will thus appear that, whatever effect the leasing and continued control of this ore on the fact of the monopolization of ore reserves may originally have had, the surrender of the lease lessened the ore holdings of the company to a point far below any possibility of monopolization. A discussion by us of the question of the possible effect of this lease as giving monopolistic control would be problematical, and the uncertain character of any conclusion reached is best emphasized by the essentially different status of the ore business now and when this lease was made. This is due to the subsequent development of other fields and to the fact that ores which a few years ago were looked upon as not usable can now be used under new methods.

We shall next consider the purchase by the Steel Company of the Tennessee Coal & Iron Company which was made in November, 1907. On the one hand, it is alleged the Tennessee company was a competitor of great power and that its purchase was for the purpose of suppressing competition and effecting mo-

nopoly and restraint of trade. On the other hand, it is contended that the competition of the Tennessee company was of relatively small extent, that its purchase was practically forced upon the Steel Company as a means of averting a threatening financial crisis during the panic of 1907, and that such purchase neither did, nor tended to, monopolize or restrain the steel and iron industry of the United States. Without here entering upon a detailed analysis of all the proofs, we have arrived at the following conclusions: At the time the Steel Company bought the Tennessee company, the latter's production of iron and steel was 1.7 per cent of the production of the country. That up to that time the Tennessee company had not been a business success. That it was making rails, which was its principal steel product, at a loss. That its ultimate success was problematic. That such success involved an outlay of upwards of $25,000,000 to put it on a dividend basis. That it had never really earned any dividends up to the time of its sale. That the whole testimony shows its relation as a successful, substantial competitor with the Steel Company in the volume of its business, the character of its product, and the breadth of its market, was negligible. We are warranted by this testimony, and find the fact to be, that its purchase by the Steel Company in no way tended to monopolize the steel and iron trade, and that it was not bought with the purpose or intent of monopolizing, or attempting to monopolize or restrain, that trade. Such negative conclusions and findings are confirmed by the affirmative proofs showing just how the purchase was made, namely, as a necessary part of comprehensive plans of bankers and business men, sanctioned by President Roosevelt, to check the panic of 1907, which was then at its height.

Indeed, as to this purchase, as well as the others, which we have discussed above, sales made under different circumstances and for various reasons, we cannot but feel, in the light of the proofs, that they were made in fair business course, and were, to use the language of the Supreme Court in the Standard Oil case, "the honest exertion of one's right to contract for his own benefit, unaccompanied by a wrongful motive to injure others."

We take up next the subject of the "Gary Dinners," which (as already stated) we have reserved for separate treatment. We use the term to cover a comparatively short period, beginning at an exceptional business situation, and continuing until normal conditions were reëstablished. These dinners — which were business meetings with a social aspect — began in November, 1907, and were held at irregular intervals during the next 15 months, and perhaps a later date. Probably it will be sufficient to say that, whether the period was longer or shorter, the element that marks it and calls for consideration now is what may be called the "coöperation" of the Steel Corporation with a large number of independent competitors, who, it will be noted, are not made parties to this bill, and who comprise some 45 per cent of the steel and iron industry of the United States. This is the only instance of such coöperation, and the whole movement was exceptional. There is some dispute in the briefs concerning the essential characteristics of these meetings, but, in our opinion, the real facts appear with sufficient clearness.

We may begin the discussion by quoting the government's concession in the original petition:

> It is not here alleged that merely assembling and mutually exchanging information and declaration of purpose amount to an agreement or a combination in restraint of trade.

With this concession we are in full accord. In these days every large business has its societies and associations, and these meet periodically to exchange information of all kinds, to compare experiences, to take note of improvements in machinery or process, to discuss problems, and generally to profit by the interchange of ideas and the study of observed facts. When the business is manufacturing, of course, all this has a direct bearing on the subject of prices, and these conferences may therefore consider that subject specifically. It is probably unusual, however, to find such a meeting making a declaration of intention to charge such and such prices, although a mere declaration to that effect could hardly be regarded as unlawful. Freedom of speech and freedom of individual action are justly prized in American society, and no legislation forbids men to come to-

gether and speak freely to each other about every detail of their common business. And if each individual should choose to announce at such a meeting the specific price he intends to charge for his wares, we are aware of no law that forbids him so to do. But at this point we approach debatable ground, for an individual is permitted to do some things that are denied to an association of individuals; and where at a meeting of many persons such action is taken whose legality is afterwards called in question, the decision may be vitally affected by ascertaining the fact whether the action was really taken by each individual acting for himself, or whether those present were, in fact, pursuing a common object.

This country has always been committed to the principle of fair and real competition in business — the struggle between individuals to sell goods in a market free from artificial control or influence — and the Sherman Act merely repeats this principle when it condemns, in the first section, "every contract or combination in restraint of trade." When, therefore, individuals or corporations make distinct contracts with each other, either in the form of pools or other agreements, dividing territory, limiting output, or fixing prices, there can be no question about the illegality of such contracts. And it makes no difference whether or not the agreement attempts to fix a penalty for its breach. The essence of the offense is that agreement; the penalty is merely an incident; so that a so-called "gentlemen's agreement" to divide territory, etc., is quite as illegal as a formal pool with a formal penalty. In a gentlemen's agreement the sanction is the sense of honor, the moral obligation, the indefinite, but real, force that in some instances compel persons to keep their promises simply because thay have promised.

But suppose what happens is this: A number of persons take no action about territory or output, their discussions being mainly concerned with the subject of price, and suppose, further, that they refrain from making a definite formal agreement, and limit themselves to an understanding, a declaration of purpose — an announcement of intention — what, then, is to be said? Have they offended against the law? This question cannot be answered until we know what the participants were really doing.

It is not enough to rest upon the varying names that may be given to the transaction. It is of the utmost importance to know how these names are to be interpreted, and this is the crucial matter to be looked for in the present record. Fortunately we find no material dispute on this point after we get below the mere surface of much that has been said by the witnesses.

The first Gary Dinner was held in November, 1907, at a time of unusual financial danger, when the threat of a serious panic was still in the air, and when ruin to many important interests was by no means improbable. The meeting was attended by representatives of from 90 to 95 per cent of the iron and steel trade, including the corporation and a large majority of its competitors, and the course of the meeting has been described by several of those in attendance. Charles M. Schwab, now president of the Bethlehem Steel Company, testified:

The steel trade promised to become in a very demoralized condition. . . . Prices had gone very low. There was a very scant demand for steel. As I stated before, many people had their warehouses full of steel. When I say there was a demoralized condition, I mean people felt that the market was going to go very low, and they were loaded with stocks. In general, there was a very uneasy feeling throughout the whole situation.

Q. To what class was this situation—to what class, I mean, of persons interested in the steel industry, was this situation — particularly threatful?

A. To the people who had stocks; the merchants of steel, the sellers of steel, the retailers.

Q. The middlemen or merchants; the retailers?

A. Exactly; the warehousemen.

Q. Were they especially loaded up at that time?

A. They were. . . . *A.* The keynote of the whole dinner was an address by Judge Gary, or rather a talk to all the members there, with a view of their not becoming panic-stricken; with a view of their not sacrificing the situation by too great a cut in prices, and a precipitation of bad business methods; that we ought to retain our heads and not become excited over a situation of that sort, and that we should calmly await the return of prosperity; that our usual pro rata of business would probably come to each one regardless of the prices at which it

was done; and that it was unwise business policy and bad for the industry, and especially bad for the people who carried stocks to precipitate and make worse such a demoralized condition. That was the keynote of everything that was said at that dinner.

Q. Was anything said about entering into an agreement fixing prices or output?

A. Nothing whatever.

Q. Were prices mentioned?

A. Not at all.

Q. Was any price of any product mentioned?

A. No; not at all.

Q. I mean a definite price for a definite product.

A. It was not discussed at all.

Q. Only a general talk along the line mentioned?

A. Just a general talk along the lines indicated.

Q. Was it voted to appoint a general committee or subcommittees at that meeting to study and take care of the situation?

A. I do not know whether those committees were appointed at the first meeting or not, but they were ultimately, I know. Committees were formed of people in the various lines of industry, people familiar with that particular line of industry, to take up in detail the keynote expressed at the first dinner.

We think it likely that, if this first meeting had not been followed by others and by the appointment of committees to continue the association (loose as it was) that resulted from that meeting, no complaint would be heard from the government. But we think the evidence makes it plain that a period of co-operation, or action with a common object, did begin in November, 1907, between the Steel Corporation and the great majority of its independent competitors, and that this period was chiefly marked by an understanding concerning the maintenance of price. Other matters were discussed at various meetings, but the principal concern was the subject of prices, and other subjects were subordinate.

Now to our minds the testimony taken as a whole makes the conclusion inevitable that the result of these meetings was an understanding about prices that was equivalent to an agreement. We have no doubt that among those present some silently dissented and went away intending to do what they pleased;

but many, probably most, of the participants, understood and assented to the view that they were under some kind of an obligation to adhere to the prices that had been announced or declared as the general sense of the meeting. Certainly there was no positive and expressed obligation; no formal words of contract were used; but most of those who took part in these meetings went away knowing that prices had been named and feeling bound to maintain them until they saw good reason to do otherwise, and feeling bound to maintain them even then until they had signified to their associates their intention to make a change. We cannot doubt that such an arrangement or understanding or moral obligation — whatever name may be the most appropriate — amounts to a combination or common action forbidden by law. The final test, we think, is the object and the effect of the arrangement, and both the object and the effect were to maintain prices, at least to a considerable degree.

We have said that this was the effect intended, and we believe it to be true, also, that in actual effect prices were more or less maintained. But it is quite as true that a large section of the trade paid little attention, if any, to this effort at coöperation. We need not quote again from the record to establish this point, for we have already made sufficient extracts earlier in this opinion. The testimony quoted on pages 84 to 88, will make it abundantly clear, we think, that, even during the period of coöperation, the prices announced and informally assented to at these meetings were not regarded at all by many manufacturers; for it is plain that the consumers who testified had no difficulty buying at rates sensibly below the prices thus referred to. It is only fair to add that in our opinion the participants in this movement did not intend to act illegally. No doubt they did intend to exercise their full legal rights, but, of course, such exercise could not be wrong, and they believed they had succeeded in keeping within the proper limits. For the reasons given, we think they were mistaken; but we acquit them of trickiness or attempted evasion.

But the period of coöperation had passed away before the bill was filed, and as far as we can see it is not likely to be repeated. We do not think the Gary movement would justify us in impos-

ing so drastic a penalty as the dissolution of the corporation; but we will, if the government moves for such action, retain the bill for the purpose of restraining any similar movement by the defendants that might be contemplated hereafter. We may perhaps suggest that under recent legislation Congress may have provided a sufficiently inclusive remedy for any future action that might have for its object the adoption or the maintenance of unreasonable prices.

In brief, the conclusions of the court are these: As to some of the defendants it is apparent the bill should be dismissed. Concerning the principal relief sought against the corporation and its subsidiaries, we are of opinion that the government has not made out a case that should be followed by a decree of dissolution, and we are also of opinion that sufficient reasons have not been afforded to justify us in now awarding an injunction. But, as already stated, if the government so desires, the court will retain jurisdiction of the cause for the purpose above outlined.

Woolley, Circuit Judge, with whom Hunt, Circuit Judge, concurs.

* * * * * * * *

My conclusions of fact and of law are that the *organizers* of the corporation (1) intended to create a monopoly and to restrain trade, and (2) combined with others and attempted to monopolize trade, within the meaning of the act, and that the *corporation* (1) neither attempted nor possessed the power alone to do the unlawful things intended by its formation, but (2) that it unlawfully combined with others to restrain trade by controlling prices.

Whatever remedy there may be against the organizers of the corporation for acts violative of the statute, certainly in this proceeding in equity a decree of dissolution cannot be awarded against the corporation for the unlawful intent and the unsuccessful attempt of its organizers to violate the law. Upon the finding that the corporation, in and of itself, is not now and has never been a monopoly or a combination in restraint of trade, a decree of dissolution should not be entered against it. Having found, however, that the corporation violated one of the provisions of the statute by combining with others to unduly restrain

trade, and that it possesses the power to again unlawfully combine with others to do the same unlawful acts, and though not actively threatening, yet because of the disposition displayed throughout the larger portion of its history, it may again do so, I am of opinion, that the corporation should be prevented doing the things and repeating the practices respecting the fixing and maintaining of prices herein viewed illegal. The ordinary relief, obviously, is the injunction process of the court, which, in an ordinary situation, would follow such a finding as of course. I am satisfied, however, that the same end will be attained, in a manner consistent with recent legislation, by retaining jurisdiction of the bill, if desired by the government, for the purpose of restraining the defendants against engaging in the price fixing practices found illegal.

VI

UNITED STATES STEEL CORPORATION FINANCE[1]

CAPITALIZATION AND INVESTMENT IN 1901

THE relation of the assets and actual investment of this great combination to the securities issued is of high public importance in estimating both the status of the Corporation itself, the reasonableness of its profits, and its other effects on the interests of the public.

The Corporation in 1901, after its organization had been fairly completed (and including the acquisition of the Shelby Steel Tube Company, which did not occur until August), had a total outstanding capitalization, including underlying bonds, sundry mortgages, and purchase-money obligations (but excluding $535,407 unacquired stock of subsidiaries), as follows:

Preferred stock	$510,205,743
Common stock	508,227,394
Steel Corporation bonds	303,450,000
Underlying bonds	59,091,657
Purchase-money obligations and real-estate mortgages	21,872,023
Total	$1,402,846,817

For the purposes of the Bureau's investigation it was essential to make an analysis of the actual value of the physical properties of the Corporation in 1901, upon which this huge capitalization was based. The Bureau has made such an analysis by three different methods:

First, by organization history — that is, from historical study of the organization and investment of the constituent concerns at the time of their formation.

Second, by market value of securities — that is, by computation of the public estimate of the value of the properties of those

[1] From U. S. Commissioner of Corporations, Report on the Steel Industry, Vol. I, July 1, 1911, pp. 14–38, 239–251, 40–60.

constituent concerns as reflected in the market prices of their securities.

Third, by departments of business — that is, by a detailed estimate of the physical properties of the company by departments of its business, computed from all available data and with an especially elaborate calculation of the value of the ore property.

The valuation arrived at by the Bureau by the first method, which is chiefly for tangible assets, is approximately $676,000,000; the valuation arrived at by the second method, which includes intangible considerations, is approximately $793,000,000; the valuation arrived at by the Bureau by the third and more precise method, this being for tangible assets only, is approximately $682,000,000.

None of these valuations includes any value imparted to these properties by the very act of merging them into the Steel Corporation and treating them as a unified going concern. Obviously such a value must be largely due to the element of concentration of control and consequent elimination of competition, which value should not be included in the present discussion.

It may be noted at this point that the United States Steel Corporation is a holding company, practically its entire property consisting of the securities of a number of subsidiary concerns, some of which, moreover, in turn own stocks in underlying concerns. For the sake of brevity and clearness in this report, however, it will be convenient to refer to the physical properties thus controlled as though they were directly owned by the Corporation itself. For all practical purposes such is indeed the fact.

Estimated Value of Corporation's Property, Based on Study of Organization of Constituent Concerns

The Bureau's estimate of the value of the Steel Corporation's property, arrived at by a study of the organization of the constituent concerns — approximately $676,000,000 — includes the entire physical property and not merely the equity over and above bonded indebtedness (which indebtedness, for these constituent concerns, is assumed to represent an equivalent invest-

ment in property). It includes only a negligible allowance for intangible considerations.

In the main the valuations arrived at are based upon the method by which these constituent companies were organized. A very common basis of organization was to determine upon cash prices for the plants acquired and then to give the vendors (the owners of the plants) the option of taking the price in cash or of taking preferred stock up to the full amount of the cash option figure, with a large bonus in common stock. New cash capital frequently was raised on the same terms. The result of this method of organization was that the preferred stock of the consolidated concern at its original organization represented practically the entire value of the property acquired — certainly the entire value of the physical assets.

This was the method followed in the four "Moore" companies, viz. National Steel Company, American Tin Plate Company, American Sheet Steel Company, and American Steel Hoop Company.

In the case of at least three of these companies a considerable block of the common stock was issued to the promoters as a "commission" for their services; in the case of the American Sheet Steel Company apparently some preferred stock was also issued for this purpose.

In the organization of the American Steel and Wire Company the preferred stock likewise covered the entire value of the physical property acquired at the time of organization, all of the common stock being issued either as a bonus or for underwriting services. The same method, substantially, was followed in the organization of the National Tube and American Bridge companies.

The common stock of the Federal Steel Company, however, appears to have had some property value back of it. . . .

The valuation of the Carnegie company's property is more difficult because the organization of this concern was arranged privately by the former owners, and because its securities were never actively dealt in. The book value of the property of the old Carnegie Steel Company (Ltd.) (which had approximately a 29½ per cent interest in the H. C. Frick Coke Company) on

March 1, 1900, or just before these two concerns were transferred to the Carnegie company of New Jersey, was, roughly, $81,500,000. This book value, while correct for some of the properties of the company, undoubtedly understated the value of others, particularly the item of "investments." Using such data as were available, the Bureau has arrived at the conclusion that the tangible property of the Carnegie concern in March, 1900, was not in excess of the $160,000,000 bond issue (the company also issued $160,000,000 of stock). A suggestive fact is that in organizing the New Jersey company $125,000,000 of bonds, and a like amount of stock, were allotted for the various Carnegie steel properties, and $35,000,000 of bonds and an equal amount of the stock for the H. C. Frick Coke Company. This clearly is analogous to a similar distribution of preferred and common stock in the case of several of the other constituent concerns of the Steel Corporation. These terms, in connection with other evidence presented in the body of the report, indicate that the Carnegie interest issued bonds up to subtantially the full amount of tangible property, leaving the stock to cover intangible considerations.

The Lake Superior Consolidated Iron Mines has been entered in the Bureau's estimate at a value equal to the par of its outstanding stock, approximately $29,400,000. . . .

The foregoing valuations, it should be kept in mind, are applicable at the dates of the respective organizations of the companies named, except in the case of the last four concerns, where the figures given apply to the dates of acquisition by the Steel Corporation. By April, 1901, the various constituent concerns had increased their property investment, through surplus earnings, to the extent of approximately $117,700,000. Adding this sum, together with $25,003,000 new cash capital provided the Steel Corporation, to the valuations stated above and including underlying bonds, purchase-money obligations, and real-estate mortgages (which also cover any additions to the property made in this way), brings the indicated total invest- in the physical property acquired by the Steel Corporation in 1901 up to approximately $676,000,000, as shown by the table on the succeeding table. [P. 19 of Report, omitted.]

Valuation of Constituent Companies as indicated by Market Prices of their Securities

The valuation of the properties of these constituent concerns arrived at by the second method of analysis is based upon the market value of their securities. Using average weekly prices, where available, and again adding underlying bonds, purchase-money obligations, and real-estate mortgages, at par, as well as $25,003,000 of new cash capital provided for the Steel Corporation, the indicated valuation is approximately $793,000,000, as shown in the table on the next page. [P. 20 of Report, omitted.]

When it is taken into consideration that these market prices include, of course, an allowance for earning power and other intangible considerations, this total of $793,000,000 indicates that the preceding valuation of $676,000,000 for the tangible property alone is sufficiently liberal.

Estimated Valuation of Property of Steel Corporation in 1901 by Departments of its Business

Both of the foregoing estimates are necessarily somewhat general. The estimate of the Bureau, based on the third method stated — that is, by departments of the Corporation's business — was prepared on a more detailed basis.

Before proceeding to discuss this estimate, it should be noted that the Steel Corporation itself, in July, 1902, in litigation then pending, submitted an estimate of the value of its assets, by principal departments, as follows:

ESTIMATE OF VALUE OF TANGIBLE ASSETS OF UNITED STATES STEEL CORPORATION ON JULY 1, 1902, SUBMITTED BY THE CORPORATION IN THE "HODGE" SUIT[1]

Ore properties	$700,000,000
Plants, mills, fixtures, machinery, equipment, tools, and real estate	300,000,000
Blast furnaces	48,000,000
Coal and coke	100,000,000
Transportation properties	80,000,000
Natural gas fields	20,000,000
Limestone properties	4,000,000
Cash and cash assets	148,291,000
Total	$1,400,291,000

[1] Chapter VII, *infra*.

This estimate of the Steel Corporation was submitted for the purpose of defending its huge capitalization, which was then directly challenged as one of the vital issues in the suit. As the legal right of the Corporation to carry out a proposed conversion of a portion of its preferred stock into bonds was dependent upon the amount of its assets there was a great inducement before the Corporation to overstate the value of its property in order to justify its capitalization. As shown later some of the Corporation's figures greatly exaggerated the true values.

The Bureau for the purposes of this third method of analysis has used the classification of property employed by the Corporation, shown in the preceding table. The basis of the Bureau's estimates by the different classes may now be briefly explained. For convenience in discussion the value of the ore property will be taken up last.

Manufacturing Properties

For most of the subsidiary companies of the Steel Corporation the Bureau's valuations of the manufacturing plants were arrived at by deducting from the par value of the preferred stock issued at their respective organizations the amounts of working capital provided. The preferred stock, as already shown, in most cases represented the total assets acquired, which in several instances consisted exclusively of plants and working capital. Therefore the values of the plants could be arrived at by deducting the working capital from the amount of preferred stock. As the properties were acquired as going concerns, the preferred-stock issues probably included in some cases an allowance for intangible considerations, and this method may therefore somewhat overstate the value of the plants. This method was used in the case of the American Steel and Wire Company, the National Steel Company, the American Tin Plate Company, the American Steel Hoop Company, the National Tube Company, and the American Bridge Company. In the case of the National Steel Company, an addition of $2,561,000 was made on account of bonded indebtedness, which

was considered as representing an equivalent investment in manufacturing properties. (Additional bonds were subsequently issued by this company, but almost entirely for other kinds of property.) A few of the other concerns had small amounts of indebtedness, bringing the total addition on this account up to $3,000,000. In the case of the American Sheet Steel Company, owing to evidence that even the preferred stock was heavily "watered," the value of the manufacturing plants was fixed at $12,000,000, although the preferred-stock issued was, roughly, $24,500,000. An addition of $1,000,000 was made to cover certain detached real estate. This company had $2,000,000 of bonded debt, but this has been considered as representing its natural-gas property.

The value given the plants of the Carnegie company was the book value, as shown in the balance sheet of March 1, 1900. In the case of the Federal Steel Company, likewise, the value for its Illinois Steel Company plants was the book value at the time of their acquisition, while the value taken for its Lorain and Johnson companies' plants was practically the cash equivalent paid. The bond issues of these concerns, therefore, do not have to be considered.

The Shelby Steel Tube Company plants have been valued at $3,000,000.

The other constituent companies mentioned in the list did not have any manufacturing plants.

The valuations thus arrived at are summarized in the table on the following page.

This total of $196,654,000, it should be emphasized, is the indicated value of the manufacturing plants and accompanying real estate at the respective dates of organization of these constituent concerns (except in the cases of the American Bridge and Shelby Steel Tube companies), and not the value at the time of transfer to the Steel Corporation. As shown above, the aggregate surplus earnings of all the subsidiaries from the dates of their respective organizations to April 1, 1901, were approximately $117,700,000. A part of this was invested in manufacturing properties, and a portion of the original working capital of these concerns was also used for this same purpose.

BUREAU'S ESTIMATE OF INVESTMENT OF CONSTITUENT COMPANIES OF UNITED STATES STEEL CORPORATION IN MANUFACTURING PLANTS (INCLUDING BLAST FURNACES) AND REAL ESTATE AT THE DATES OF THEIR RESPECTIVE ORGANIZATIONS

COMPANY	PREFERRED STOCK ISSUED	CURRENT ASSETS AT ORGANIZATION	BALANCE TO REPRESENT PLANTS
American Steel and Wire Company	$40,000,000	$16,000,000	$23,400,000
National Steel Company[1]	27,000,000	9,000,000	18,000,000
American Tin Plate Company[1]	18,325,000	4,500,000	13,825,000
American Steel Hoop Company	14,000,000	3,000,000	11,000,000
National Tube Company	40,000,000	16,000,000	24,000,000
American Bridge Company[1]	31,374,000	11,500,000	19,874,000
Other companies:			
Carnegie Company (book value)	—	—	43,355,000
Federal Steel Company —			
Illinois Steel Company (book value)	—	—	20,200,000
Lorain and Johnson companies (approximate cash price)	—	—	4,000,000
Shelby Steel Tube Company (approximate cash price)	—	—	3,000,000
American Sheet Steel Company (estimated)	—	—	13,000,000
Add to cover investment in manufacturing plants represented by miscellaneous bonds	—	—	3,000,000
Total	—	—	196,654,000

Just how much was invested in manufacturing plants is not definitely known. Large sums were invested in ore, coal, and transportation properties. On the other hand, there had very likely been some depreciation of these properties. From various data obtained the Bureau has concluded that an allowance of $250,000,000 would be sufficient to cover the total investment in these manufacturing properties on April 1, 1901. (Only a small addition had to be made on account of additional securities issued, because these were almost exclusively for other classes of property.)

That this allowance of $250,000,000 is sufficiently liberal is

[1] In the case of this company the preferred stock here given includes a small amount issued soon after the organization of the company.

indicated by data furnished by the Steel Corporation. At the close of December, 1907, the Steel Corporation made an appraisal of its assets (omitted), in which the manufacturing properties (other than the Gary plant and those of the Tennessee Coal, Iron and Railroad Company) were valued at $367,600,000. This figure, according to the Corporation, represented the construction cost less accrued depreciation (omitted), except for real estate, which was taken at the current value. During the period from April 1, 1901, to December 31, 1907, there had been invested in net capital additions to these manufacturing properties (again excluding the Gary and Tennessee plants) approximately $114,500,000. Deducting this from the foregoing figure, gives an indicated investment in these manufacturing properties in April, 1901, of $253,000,000. This amount was over and above an expenditure of approximately $180,000,000 for ordinary maintenance and repairs which, in some cases, apparently included an allowance for depreciation although not so designated.

The Corporation's valuation of $367,600,000 at the end of 1907, however (and consequently the resulting figure of $253,000,000 for 1901), includes real estate at values in excess of those prevailing in 1901. Allowing for this fact, this 1907 appraisal of the Corporation does not indicate a valuation for the Corporation's plants in April, 1901, in excess of $250,000,000.

Summary for Property other than Ore

The Bureau's estimates of the tangible property of the Corporation, other than ore, in 1901, are therefore as follows:

Manufacturing, including blast furnaces	$250,000,000
Transportation	91,500,000
Coal and coke	80,000,000
Natural gas	20,000,000
Limestone	4,000,000
Working assets	136,500,000
Total	$582,000,000

The total value assigned these classes of property in the Corporation's estimate of 1902 (see table omitted), it will be observed, was roughly $700,000,000, or, after including the

bonded indebtedness of transportation properties and purchase-money obligations and mortgages, to make the two estimates fairly comparable, approximately $757,000,000. The Corporation's estimate, of course, included additions to property made from April 1, 1901, to July, 1902. Nevertheless the Corporation's estimate of its manufacturing properties was undoubtedly excessive. Except in this instance, the Bureau's valuations for these classes of property are not strikingly different from those of the Corporation in 1902.

Value of the Ore Property of the Steel Corporation

The ore valuation made by the Corporation, however, presents a very different question. The table on page 189 shows that the Corporation assigned a value of no less than $700,000,000 to its ore property, or almost one half of the total claimed for all its assets. It is evident, therefore, that conclusions regarding the value of the ore must largely govern opinions as to the relationship between the capitalization and the actual property assets of the Steel Corporation as a whole.

The Bureau has estimated the value of this ore property by three different methods — first, on the basis of prices paid for ore in fee shortly before the Corporation was organized; second, on the basis of the price paid by the Steel Corporation itself for a certain portion of its ore property; and, third, by a calculation of the "present worth" of royalties on leased ore.

Comparing the Bureau's estimates of this ore property by the several methods described, it will be seen, first, that the current prices of fee ore indicate that the fee properties and leaseholds of the United States Steel Corporation were worth much less than $90,000,000; second, that the terms of the purchase of the Lake Superior Consolidated Iron Mines indicate a total value for all the ore property of the United States Steel Corporation in 1901 of not over $70,000,000 to $94,000,000; and, third, that the valuation based on present worth of royalties and bonus values of leases indicates that the same property was worth about $90,000,000.

Altogether there can be no doubt that an estimate of from

$90,000,000 to $95,000,000 as the value of this ore property would be sufficiently high. Taking all the facts into consideration, however, the Bureau concluded to allow a round value of $100,000,000 for the ore property in 1901.

It is worth calling passing attention to the fact that in the year 1902 the total valuations, as assessed for taxation, of all iron-mining properties in the States of Minnesota and Michigan, of which at that time the United States Steel Corporation probably owned not much over one half, was only about $54,000,000. Practically all the Corporation's ore holdings were then in these two States. In other words, the Corporation's ore property, which, for taxation, was probably assessed at considerably less than $40,000,000, was, for the purpose of justifying its capitalization, valued at $700,000,000. Of course, it is not intended to say that the tax valuations represented the full value of the property.

Summary of Bureau's Valuations by Departments of the Business

The valuations for the different classes of the property of the Corporation in 1901, arrived at by the Bureau by this third method, are in the following table summarized and compared with those of the Corporation in 1902, as already given on page 189.

Value of Tangible Assets Acquired by Steel Corporation in 1901, as computed by Bureau, compared with Estimate of Corporation submitted in the Hodge Suit in July, 1902

Class of Property	Bureau's Estimate of Tangible Values in 1902	Corporation's Estimate of Tangible Values in 1902	Difference
Ore property	$100,000,000	$700,000,000	$600,000,000
Manufacturing plants, including blast furnaces	250,000,000	348,000,000	98,000,000
Railroad, steamship, and dock property	91,500,000	120,340,000	28,840,000
Coal and coke property	80,000,000	100,000,000	20,000,000
Natural-gas property	20,000,000	20,000,000	—
Limestone properties	4,000,000	4,000,000	—
Cash and cash assets	136,500,000	164,660,000	28,160,000
Total	682,000,000	1,457,000,000	775,000,000

The total valuation of $682,000,000, it will be seen, is less than one half the value claimed by the Corporation in 1902. Nevertheless, in every case the valuations of the Bureau are believed to be liberal. As already noted, the estimates of the Corporation include additions to the property up to July 1, 1902. Such additions, however, would explain only an insignificant part of the discrepancy, and, in the case of the ore, are entirely negligible.

It may be repeated that the Bureau's figures do not allow for any additional value which may have been imparted to these properties by the mere act of consolidation. A large part of any such addition is properly excluded from consideration, as it must have been due in a measure to concentration of ownership and control or the restriction of competition. While the merger of such properties, particularly on account of greater integration, might have imparted a considerable value to them as going concerns over and above the aggregate of the valuations prior to consolidation, it is impossible to separate any such increase in value, due to coördination and integration, from the increase due to the elimination of competition, and therefore no quantitative statement of such additional value has been attempted by the Bureau.

Comparison of Valuations of Steel Corporation's Property in 1901 with its Capitalization

The Bureau's valuations of the Steel Corporation's property in 1901, arrived at by these different methods, may now be compared with its outstanding capitalization at that time. This is done in the table on opposite page.

It will be seen at once that the securities issued by the Steel Corporation very greatly exceeded the indicated value of the property acquired, as established by any one of the three methods of valuation. The valuation of the tangible property arrived at by historical study, as well as that by departments of the business, shows an excess of capitalization greater than the indicated value itself. The valuation by departments, namely, $682,000,000, shows an excess of nearly $721,000,000. Even tak-

COMPARISON OF ESTIMATES OF VALUE OF PROPERTY OF UNITED STATES STEEL CORPORATION AT ITS ORGANIZATION IN 1901, WITH PAR VALUE OF ITS SECURITIES

		EXCESS OF SECURITIES OVER ESTIMATES
Total capitalization in April, 1901, including underlying bonds and purchase-money obligations .	$1,402,846,817	
Investment in tangible property alone, indicated by historical analysis	676,000,000	$726,846,817
Value of all property, tangible and intangible, as indicated by market prices of securities of constituent concerns	793,000,000	609,846,817
Value of tangible property as estimated by departments of the business	682,000,000	720,846,817

ing the indicated market value of the securities of the subsidiary concerns, namely, $793,000,000, which valuation includes the public estimate for intangible considerations as well as physical property, the excess of the Steel Corporation's capitalization was still over $609,000,000. Naturally the valuation arrived at by this method exceeded those obtained in the other two cases.

The Bureau does not contend that the capitalization of the Steel Corporation should have been fixed at any one of the three valuations here presented. All that is attempted at the moment is to present a comparison of these valuations with the capitalization. The figures show clearly that the entire issue of approximately $508,000,000 of common stock of the Steel Corporation in 1901 had no physical property back of it, and also a considerable fraction, say from one fifth to two fifths, of the preferred stock was likewise unprotected by physical property. Even granting that there may have been a considerable value in intangible considerations, it is reasonably clear that at least the entire issue of common stock, except in so far as what may be termed "merger value" may be considered, represented nothing but "water."

While, therefore, it is not the purpose of this report to say what should have been the capitalization of the Steel Corporation, it is obvious that the company was heavily overcapitalized, judged by any reasonable standard.

EXCESSIVE ISSUE OF SECURITIES BY UNITED STATES STEEL CORPORATION IN 1901

Comparison of Bureau's Valuation with Total Outstanding Capitalization

The Bureau's estimates of the value of the investment of the United States Steel Corporation at its organization in April, 1901, arrived at by the three different methods employed — that is, by analysis of the assets of the constituent concerns, by the use of market quotations of securities of those concerns, and by departments of the business of the Corporation itself — may now be summarized and compared with the capitalization of the Corporation at that time. Such a comparison is given in the following table:

Comparison of Estimates of Value of Property of United States Steel Corporation at its Organization in 1901, with Par Value of its Securities

		Excess of Securities over Estimates
Total capitalization in April, 1901, including underlying bonds and purchase-money obligations . .	$1,402,846,817	
Investment in tangible property alone, indicated by historical analysis	676,000,000	$726,846,817
Value of all property, tangible and intangible, as indicated by market prices of securities of constituent concerns	793,000,000	609,846,817
Value of tangible property as estimated by departments of the business	682,000,000	720,846,817

The Bureau's two valuations of the tangible property alone agree very closely, although to a very considerable extent they were arrived at independently of one another. The valuation based on market prices of the securities of the constituent concerns naturally is higher than the other two, since it includes intangible considerations as well.

It will be seen at once that the capitalization of the Steel Corporation in 1901 greatly exceeded the value of the property acquired as indicated by any one of the three methods

employed. By the first method, that of historical analysis of the organization of the constituent concerns, the excess of capitalization over tangible assets was, roughly, $727,000,000. By the third method, which also considers tangible assets only, the excess is $721,000,000. Even on the basis of the second method, which, as repeatedly pointed out, is the public's estimate, through the stock market, of the value of the companies as going concerns and which therefore includes intangible as well as tangible assets, the excess is nearly $610,000,000.

Owing to the difficulty, and, indeed, to the practical impossibility, of arriving at a valuation of the intangible assets of the Corporation which would not be influenced by the element of combination the Bureau has confined its study of the investment to tangible property. For this purpose it has accepted the valuation of $682,000,000 arrived at by the third method, in the manner already described in the preceding chapter. While, of course, absolute precision cannot be claimed for this figure, it was reached only after very exhaustive analysis; moreover, in every case the Corporation was given the benefit of reasonable doubt, so that this result must be regarded as distinctly a liberal valuation of the tangible property of the Corporation in 1901. On this basis, no less than $720,846,000 of the total capitalization of the Corporation was unprotected by tangible property values; that is to say, the entire issue of, roughly, $508,000,000 of common stock and over $212,000,000 of the preferred stock had no tangible property back of it at the organization of the Corporation in 1901.

In this connection it may be noted that in testimony before the Ways and Means Committee, in 1908, E. H. Gary, chairman of the Steel Corporation, was questioned with respect to a valuation of $1,782,187,383 for the properties of the Steel Corporation at the close of 1907. An excerpt from his testimony before that committee follows:

MR. COCKRAN. Of this whole sum of $1,782,000,000, was not $1,000,000,000, at least, capitalized profits as distinguished from original investment?

MR. GARY. I should have to guess at that; but I should guess yes, including increases in value.

While an offhand answer to such an important question should not be given too much weight, the resulting valuation of, say, $782,000,000 for the properties at the time the Steel Corporation was formed is surprisingly in line with the valuation of the Bureau already given.

The Bureau does not for the purposes of the present discussion take up the question whether the Steel Corporation should have issued securities up to only the value of the tangible property, as here estimated. As previously pointed out, opinions concerning the proper basis of capitalization are very diverse. The Bureau is not concerned at the moment with the question of what would be the best method of capitalization, but with the relation between the capitalization actually determined upon and the value of the investment represented thereby. The question of the principles of capitalization is one of great general interest, but in this present discussion the Bureau is dealing only with the question of fact. On this point, as already stated, it is clear that there was an excess of more than $700,000,000 of capitalization over the actual investment in tangible property in 1901. Even granting that there may have been a considerable value in the intangible considerations, it is reasonably clear that at least the entire issue of common stock, setting aside all "merger value," represented nothing but "water."

While, therefore, it is not the purpose of this report to say what should have been the capitalization of the Steel Corporation, it is obvious that the company was heavily overcapitalized, judged by any method of valuing its assets.

Comparison of Par Value of Securities of Steel Corporation itself with their Market Value

Incidentally it is well to consider briefly the aggregate market value of the securities of the Steel Corporation itself. But it must be clearly recognized that this is in no sense a part of the previous discussion of the value of its assets, because such a computation introduces a wholly new factor, namely, the merger value given to the properties by the very act of combining them under a single great concern, and other intangible considerations.

The average price at which United States Steel preferred stock sold during the first year of the existence of the Corporation—this average being based on an average of the means of the highest and lowest quotations daily—was 94, and the corresponding average for the common stock was 44. The average price of the 5 per cent fifty-year bonds was approximately 115. The average price of the underlying bonds, mortgages, and purchase-money obligations cannot be satisfactorily determined. Since transactions in some of these were very infrequent, and in some cases there were no recorded transactions, and since the total amount of these was comparatively small, they may be reckoned at par, as they have been in preceding tables of this sort.

Applying these average prices to the total outstanding capitalization of the Steel Corporation (including underlying bonds, mortgages, and purchase-money obligations) at the time of its organization, the indicated market valuation of these securities was approximately $1,133,144,631, as shown by the following table:

COMPARISON OF PAR VALUE OF STEEL CORPORATION'S SECURITIES WITH MARKET VALUE, BASED ON AVERAGE PRICES FOR THE FIRST YEAR AFTER ITS ORGANIZATION

Security	Par Value	Average Price First Year	Market Value Based on Average Price First Year	Excess of Par Value over Market Value
Preferred stock	$510,205,743	94	$479,593,398	$30,612,345
Common stock	508,227,394	44	223,620,053	284,607,341
5 per cent bonds	303,450,000	115	348,967,500	*45,517,500*
Underlying bonds, mortgages, and purchase-money obligations	80,963,680	100	80,963,680	——
Total	1,402,846,817	——	1,133,144,631	269,702,186

The par value of the Steel Corporation's securities, therefore, shows an excess over the market valuation of $269,700,000. Had the fifty-year bonds been taken at par instead of at the

market value (which method might be justified on the ground that the premium was largely influenced by the term of these bonds, and the condition of the money market rather than by property values), the excess would have been about $315,000,000.

It should be unnecessary, however, to argue that a market valuation based upon the prices of the securities of the Steel Corporation itself is not a proper criterion by which to judge the real value of the assets of the Corporation at its organization. It will be remembered that it was shown that the market valuation of the securities of the constituent concerns acquired by the Steel Corporation based upon the average prices of 1899 and 1900 (and including $25,003,000 new cash capital as well as underlying indebtedness at par) was $792,961,970. The market value of the securities of the Steel Corporation itself based upon the average prices recorded during the first year of its operation (except for the underlying indebtedness, which is taken at par) is $1,133,144,631, or $340,182,661 more than the market valuation of the securities acquired in the component concerns in 1899 and 1900.

It is apparent, therefore, that the aggregate market valuation was greatly increased as a direct result of the merger of these various constituent concerns under a single control. Undoubtedly much of this increase in market valuation was in the nature of an increase due to concentrated control over the industry. It is incredible that there had been any such enormous increase in the real value of the property in this short interval. A part of the increase was undoubtedly a temporary reflection of current conditions in the stock market. The year 1901 was one of marked prosperity in the steel industry, and despite the acute stock-market panic which occurred in May it was a year of firm and even of rising values for securities in general. The stocks of the Steel Corporation, moreover, undoubtedly were given support by large banking interests during the greater part of the organization period. In view of these facts, and more especially the fact that the Steel Corporation was a consolidation controlling a very substantial proportion of the steel business of the country, this market valuation of its securities of approximately $1,133,000,000 obviously exaggerates

a fair valuation of the properties acquired as they existed under separate ownership. Nevertheless, even judged by this unduly favorable standard, the capitalization of the Corporation was very excessive.

It may be noted in this connection that in the latter part of 1903 and the early part of 1904, during a sharp reaction in the steel industry, the market value of its securities was very greatly reduced. Thus the preferred stock in 1903 sold as low as $49\frac{3}{4}$, and the common stock as low as 10 (the latter sold somewhat lower in 1904). The fifty-year bonds sold as low as 102, while the new 10–60 year bonds, which were issued in that year chiefly to retire preferred stock, sold as low as 65. At these low prices (including underlying indebtedness at par in the absence of quotations), the total market value of the securities of the Corporation was only about $751,000,000, or $382,000,000 less than the aggregate value shown by the 1901 prices.

The Bureau does not contend that this valuation at these low prices is a fair indication of the real value of the property at that time, but this figure illustrates the danger of using stock-market quotations as a conclusive test of values unless averaged over a long period under varying conditions. On the other hand, such stock-market prices, when averaged over long periods, frequently are an exceedingly valuable criterion.

Evidence of Overcapitalization in Excessive Issue of Stock to Underwriting Syndicate

Very convincing evidence of an excessive issue of securities by the Steel Corporation is afforded by the enormous payment which it allowed the underwriting syndicate, so called. The syndicate agreement provided that in addition to undertaking to secure at least 51 per cent of the stocks of the various companies originally to be acquired, the syndicate should furnish the Steel Corporation with $25,000,000 cash capital. In addition to this sum, the syndicate incurred expenses of about $3,000,000 attendant upon the organization of the Corporation, through fees, purchase of miscellaneous securities, etc., which sum should be

added to the $25,000,000 cash capital provided, in stating the total cash consideration provided by the syndicate. For this total cash consideration of $28,000,000 and its services the underwriting syndicate received from the Steel Corporation the enormous total of practically 1,300,000 shares of its stock (half preferred and half common), of an aggregate par value of $130,000,000. That this huge block of stock was actually received by the syndicate was explicitly stated in the preliminary report of the Steel Corporation, which, after giving the amounts of stock issued to acquire the securities of the constituent concerns, further stated:

> The residue of the common and preferred stock of this Corporation delivered to the syndicate under the contract of March 1, 1901, and not used for the acquisition by it of the stocks of the specified companies, being the shares which, as stated in the syndicate circular of March 2, 1901, were to be retained by and to belong to the syndicate, amounted to 649,987 shares of preferred stock, and 649,988 shares of common stock. This residue of stock or the proceeds thereof, after reimbursing the syndicate the $25,000,000 in cash which it paid to the Corporation, and approximately $3,000,000 for other syndicate obligations and expenses, constituted surplus or profit of the syndicate.

Profit Realized from this Stock by the Syndicate. — This enormous "residue," as it was termed, yielded a very large profit to the syndicate. At valuations of 44 for the common stock and 94 for the preferred stock (the average prices, respectively, at which these shares sold during the first year after the organization of the Steel Corporation), the total value of these stocks thus delivered to the syndicate would have been approximately $89,700,000. As a matter of fact, it appears that the amount actually realized by the syndicate was about $90,500,000. After reimbursing the syndicate for the $25,000,000 cash capital raised by it, and also for the $3,000,000 incurred in expenses, the syndicate managers paid out in profits to syndicate members substantially $50,000,000. Before distributing these huge profits, however, J. P. Morgan & Co., as syndicate managers, reserved as their compensation 20 per cent of the total profits. The total profits consequently were one fourth greater

than the amount thus distributed to syndicate members, or, in other words, they were, roughly speaking, $62,500,000.

It may be noted that about $4,000,000 of this total was not in the form of cash. After reimbursing the syndicate for its cash obligations of $28,000,000, the syndicate managers paid four cash dividends of $10,000,000 each (after reserving in each case their 20 per cent commission), and a final dividend of $6,000,000 in cash plus $4,000,000 paid-up participation in a syndicate then being organized by J. P. Morgan & Co. to underwrite the so-called "bond conversion" scheme of the Corporation, discussed elsewhere. There is some question whether this $4,000,000 participation in the second syndicate realized its par value on the liquidation of that syndicate, but any difference between the amount finally realized and the par value ($4,000,000) was undoubtedly so small that it can be disregarded. The profit on this operation over and above all expenses may therefore be fairly stated at $62,500,000.

There can be no question that this huge compensation to the syndicate, or, in other words, the enormous block of stock upon which this profit was realized, was greatly in excess of a reasonable compensation. The syndicate was, of course, properly to be reimbursed not only for the $25,000,000 new cash capital which it provided the Corporation, and for the $3,000,000 of expenses incurred, but was also entitled to some compensation for the labor and risk of raising these sums. Moreover the syndicate presumably rendered some other services of value in facilitating the organization of the Corporation and the flotation of its securities, for which it would reasonably expect some compensation. However, these services certainly were not worth anything like the enormous price which the Corporation paid. Nor can this payment be justified on the ground of extraordinary risk. The Corporation was organized at a time of pronounced buoyancy in the stock market and decided prosperity in the steel industry. It is true that only a short time after its organization the famous Northern Pacific corner and the resulting stock-market panic occurred. Such a contingency, however, is one of the possibilities that all underwriting syndicates have to take account of, and was entitled to no more weight in this case

than in the case of numerous other underwriting arrangements which were made by other large corporations at the same period.

It is, moreover, true that the nominal liability of the syndicate, or what may be called its nominal capital, was $200,000,000. This, however, was the liability of the syndicate subscribers to the syndicate managers and not to the Steel Corporation, to which its cash liability, as just shown, was only $25,000,000 (not including $3,000,000 of expenses). It was the understanding, tacit or expressed, that the syndicate managers did not expect to call upon the syndicate subscribers for more than a single payment of 12½ per cent of the total nominal liability ($200,000,000), or $25,000,000. As a matter of fact, that was the only call actually made. Had a further call been made upon the syndicate subscribers, this would have been to meet temporary exigencies accompanying the flotation of the Steel Corporation's stock, and not to make any further payment to the Corporation itself. The large nominal obligation of the syndicate subscribers to the syndicate managers apparently was determined upon in part with a view to disarming subsequent criticism of the enormous compensation which it received.

A very important consideration to point out is that while the syndicate was, from the standpoint of the prestige and reputation of the bankers identified with it, nominally compelled to see the organization of the Steel Corporation successfully through, there was no legal obligation of this sort whatever. Instead, a circular of the syndicate managers to the stockholders of the various constituent concerns which were to be acquired stated very positively that the syndicate managers might at any time wholly abandon the transaction, in which event the stockholders in the acquired companies would have no claim whatever against the syndicate managers. This is shown by the fourth paragraph in the official circular of J. P. Morgan & Co., the syndicate managers, as follows:

The undersigned are authorized to proceed with the proposed transaction whenever in their sole judgment a sufficient amount of the stocks of said companies, or any of them, shall have been deposited. *They reserve the right, at any time, in their discretion, to wholly abandon the transaction* and to withdraw their offer herein contained, as to all

the depositors, by publication of notice of such withdrawal in two daily newspapers in the city of New York; and in that event all the deposited shares shall be returned without charge upon surrender of the respective receipts therefor. *In case of any such withdrawal* of the offer hereunder as to all or to any depositors, *such depositors shall have no claim against the undersigned*, and shall only be entitled to receive their deposited securities upon surrender of the respective receipts therefor.[1]

It may be objected, as just suggested, that it is almost incredible that the syndicate managers would abandon the transaction. Nevertheless, this distinct provision that they might do so if they saw fit, without giving any explanation and without rendering themselves in the slightest way liable, clearly is entitled to great weight in judging the risks assumed by the syndicate. As a matter of fact, as the sequel showed, the syndicate was compelled to bear only a very moderate risk, while it was one of the most profitable ever organized in the United States.

It is worth passing notice that J. P. Morgan & Co., the syndicate managers, in the closing paragraph of their circular to the shareholders, said:

It is proper to state that J. P. Morgan & Co. are to receive no compensation for their services as syndicate managers beyond a share in any sum which ultimately may be realized by the syndicate.

As just shown, however, the share of J. P. Morgan & Co. in the profits of the syndicate, as syndicate managers only, was about $12,500,000, in addition to whatever profits they may have made because of their participation in the syndicate as subscribers. In view of this profit, it is hardly remarkable that that firm received no further payment from the Steel Corporation itself.

In this connection it is also proper to point out that the syndicate managers were prominently identified with the management of several of the companies acquired by the Steel Corporations, and also with the management of that Corporation itself. Three partners of the firm were on the directorate of the Corporation, one of whom was also chairman of the finance

[1] Italics by Bureau.

committee. Moreover, several other leading interests in the underwriting syndicate were the heads of some of the companies acquired and members of the first board of directors of the Corporation. In other words, as managers of the Steel Corporation, these various interests virtually determined the compensation for their services as underwriters.

It may also be stated that in January, 1902, the syndicate managers proposed that a formal agreement of release be executed between themselves and the Steel Corporation concerning this syndicate operation. The following proposition was submitted to the finance committee of the Steel Corporation by the syndicate managers:

The magnitude of the transactions, and the immense amount involved under the contracts of March 1, 1901, and April 1, 1901, render it important, and it is our desire, that all matters between the Corporation and ourselves, as syndicate managers or otherwise, relating in any way to the issue of the capital stock of your Corporation and to the acquisition of the stocks of other companies, should be definitely closed and settled in such manner that no possible question concerning the same or the amounts or profits involved can be raised in the future. We desire, if practicable, that such a final settlement, which it seems to us should be by way of mutual releases, be had before we distribute the profits of the syndicate among its members.

Such an arrangement was entered into and formally approved by the directors of the Steel Corporation on February 14, 1902. At that time, it may be noted, the profits of the syndicate were estimated by the syndicate managers at about $56,000,000. This proved to be an underestimate, and, as above shown, the total profits actually realized were about $62,500,000.

In addition to the importance of this payment to the underwriting syndicate itself as indicating overcapitalization, this transaction may also fairly be given weight in discussing evidence of excessive issue of securities with respect to the purchase of properties. A corporation which issued roughly $130,000,000 of its securities for a cash consideration of $25,000,000 plus such underwriting and promotion services and expenses as were involved in this case may fairly be regarded as disposed to issue its capital stock on an exceedingly liberal basis for the acquisi-

tion of properties. This syndicate arrangement, therefore, may properly be construed as confirming other evidence that the capitalization of the Corporation far exceeded the true value of its assets.

At the invitation of the Bureau, the syndicate managers in 1911 submitted a statement concerning this compensation of the syndicate. Their statement on this point follows:

As stated in the first preliminary report of this company, submitted to its stockholders at the first annual meeting upon February 17, 1902, and then and there unanimously approved, there was allowed to the underwriting syndicate as its compensation 649,987 shares of the preferred stock and 649,988 shares of the common stock of the new corporation, out of which the syndicate provided the corporation with $25,000,000 cash and distributed approximately $3,000,000 for other syndicate obligations and expenses.

We enclose a copy of the printed syndicate agreement of February 26, 1901, under which the net profits of the syndicate were distributable, and they were distributed one fifth to the syndicate managers and the remaining four fifths to the syndicate subscribers, including our firm.

Inasmuch as these commissions and their payment were unanimously approved by the stockholders of the corporation, we should assume that your view (which we regret) that they were excessive in amount has regard, not to the parties immediately concerned, but to what you may consider to be a public interest. In this aspect it would seem to us that, if, as we believe, and as we have above stated, the properties acquired by the Steel Corporation were and are fully worth the par of the entire block of securities by it issued to the syndicate managers in payment therefor, no public injury could or would result from any subdivision between the syndicate managers and their associates of the securities so issued.

We would suggest further that, as the transaction was unique, not only in character, but in immensity, it is possible that any standard short of that furnished by practical experience of necessity must be imaginary and perhaps illusory. Contingencies and reasons involved in this so large a transaction require and justify compensation at a rate which in lesser matters might seem excessive. No ordinary experience can supply a measuring stick for either the purchase price of the properties of the new corporation or the payment of the compensation for such acquisition.

We would call attention also to the fact that the purchase price of the properties transferred under the first contract of March 1, 1901, covered the entire compensation received by the syndicate. The subsequent acquisition under the contract of April 1, 1901, of the so-called Rockefeller properties, the Pittsburg Steamship Company, and the Oliver Iron Mining Company were made by the syndicate managers not on their own account but for and in behalf of the new company, the United States Steel Corporation, and no commissions or compensation for this acquisition was asked or received by the syndicate managers.

The Bureau does not regard the above statement as an adequate defense of the enormous commission obtained by this underwriting syndicate. Undoubtedly the transaction was exceptional with respect to magnitude. This would undoubtedly justify a larger commission in the aggregate than would be justified in the case of a very small underwriting operation. Moreover, the magnitude of the operation might justify a somewhat greater allowance for contingencies, although, as already pointed out, every underwriting syndicate must run the risk of certain contingencies, such, for instance, as a violent disturbance in the stock market, or, on the other hand, a period of continued depression. So far as the above explanation of the syndicate payment rests on the assumption that the properties were worth the par value of the entire amount of stock issued therefor, it is obvious that this view cannot be accepted. As a matter of fact, if the properties themselves were regarded by the vendors as worth par, it cannot be conceded that those vendors would have been willing to surrender $130,000,000 of the entire capital stock to an underwriting syndicate, except on the ground that they expected to make such extraordinary profits out of the merger that they would thereby be reimbursed. In any event, it is obvious that any such large commission to an underwriting syndicate is a matter of vital importance from a public standpoint.

It may be noted that this statement of the syndicate managers calls attention to the fact that the entire commission was allowed under the first contract, which did not include the acquisition of the Rockefeller properties (the Lake Superior Consolidated Iron

Mines and the Bessemer Steamship Company), the American Bridge Company, and the one sixth interest in the Oliver Iron Mining Company and in the Pittsburg Steamship Company, but that no compensation was received by the syndicate managers for these later acquisitions. This simply means, however, that this syndicate commission covered the acquisition of only a part of the properties of the Steel Corporation. It may be noted in this connection that the second syndicate agreement — that of April 1, 1901 (a copy of this agreement appears on pages omitted) — contained a provision that the Steel Corporation, in addition to reimbursing J. P. Morgan & Co. for actual expenditures incurred in the acquisition of these properties thus subsequently brought in, should pay that firm "fair compensation for their services." While, according to the above statement, no such compensation was received under this second contract, this can hardly be regarded as remarkable, in view of the fact that the compensation under the first contract netted the syndicate the enormous sum of roughly $62,500,000, of which the syndicate managers received one fifth, this not including any amount which they may have received as members of the syndicate.

Summary of Underwriting Commissions in the Organization of the Steel Corporation and its Constituent Concerns

Another way of looking at this large compensation to the underwriting syndicate is that $28,000,000 of the preferred and $28,000,000 of the common stock were issued to cover the $28,000,000 cash liability and expenses of the syndicate, the common stock being regarded as a 100 per cent bonus with the preferred, as was so often done in organizing the constituent concerns. On this basis there would be left $36,998,700 of preferred stock and $36,998,800 of common stock as a "commission" in the strict sense, merely for the services of the underwriting syndicate as distinct from any cash consideration or expense.

This enormous commission to the underwriting syndicate of

the Steel Corporation, it will be recalled, followed other heavy commissions of the same sort paid by most of the constituent concerns of the Corporation. The facts concerning the payments of such commissions by the subsidiary companies have already been summarized in Chapter II. It was there shown that the total amount of stock issued by seven of the constituent concerns (this not including the American Sheet Steel Company or the Shelby Steel Tube Company) as commissions to promoters of underwriting syndicates, exclusive of bonus stock issued for property or cash, aggregated no less than $63,306,-811, of which $62,449,612 was common stock and $857,199 was preferred.

The amounts of stock thus issued as commissions by the subsidiary companies received, of course, the same terms of exchange in the acquisition of these concerns by the Steel Corporation as the other stocks of the same class. As already shown the rates of exchange in most instances were at more than par. By adding the amounts of United States Steel Corporation stock thus issued in exchange for these amounts of the stock of the constituent companies which were originally issued for commissions to the amount of the Steel Corporation's stock above, which may be regarded as such a commission in the strict sense (after deducting $28,000,000 of each class to cover the cash raised or expended by the syndicate), a total is reached which may be regarded as the amount of the Steel Corporation's stock issued directly or indirectly for promotion and organization profits. A summary of such total commissions is given in the table on opposite page.

From this table it appears, therefore, that more than $150,-000,000 of the stock of the Steel Corporation (this including over $41,000,000 of preferred stock and $109,000,000 of common stock) was issued, either directly or indirectly (through exchange), for mere promotion or underwriting services. This total, moreover, as noted, does not include anything for the American Sheet Steel Company, although presumably a large commission, possibly including some preferred stock, was obtained by the promoters of this concern, nor is anything added in the case of the Shelby Steel Tube Company.

AMOUNT OF STEEL CORPORATION'S STOCK ISSUED AS A COMMISSION TO THE UNDERWRITING SYNDICATE, AND AMOUNTS SO ISSUED IN EXCHANGE FOR STOCKS OF CONSTITUENT CONCERNS ISSUED FOR THE SAME PURPOSES, EXCLUDING IN ALL CASES STOCK ISSUED AS A BONUS FOR PROPERTY OR FOR CASH

COMPANY	AMOUNT OF STOCK ISSUED TO COVER PROMOTION CHARGES	RATES OF EXCHANGE INTO U. S. STEEL STOCK		TOTAL AMOUNT OF U.S. STEEL STOCKS ISSUED IN THIS EXCHANGE	
		Preferred	Common	Preferred	Common
Federal Steel Company:					
Preferred	$857,192	110.00	—	$942,911	—
Common	3,599,619	4.00	107.50	143,985	$3,869,590
American Steel and Wire Company, common	11,600,000	—	102.50	—	11,890,000
American Tin Plate Company, common	10,000,000	20.00	125.00	2,000,000	12,500,000
National Steel Company, common	5,000,000	—	125.00	—	6,250,000
American Steel Hoop Company, common	5,000,000	—	100.00	—	5,000,000
National Tube Company, common	20,000,000	8.80	125.00	1,760,008	25,000,000
American Bridge Company, common	7,250,000	—	105.00	—	7,612,500
Total, subsidiary companies .	63,306,811	—	—	4,846,904	72,122,090
Add for U. S. Steel Corporation, after deducting $28,000,000 of each class to cover cash provisions	—	—	—	36,998,700	36,998,800
Grand total securities of U. S. Steel Corporation representing commissions to promoters and bankers for the Corporation and its constituent concerns combined	—	—	—	41,845,604	109,120,890

It should be repeated that this enormous total of over $150,000,000 does not include common stock issued as a bonus with preferred for property or for cash, but simply what may be termed the promotion and organization commissions in the strict sense. In other words, nearly one seventh of the total capital stock of the Steel Corporation appears to have been issued, either directly or indirectly, to promoters for their services.

ADDITIONS TO PROPERTY SINCE 1901

Since 1901 the Steel Corporation has greatly increased its investment. The increase has come about in two ways — first, and most important, through new construction and additions by the investment of surplus earnings and new capital derived from the sale of securities; and, second, through the acquisition of competing concerns through issue of securities directly therefor.

* * * * * * * *

By combining the net additions to fixed property made through direct expenditure and through such acquisitions, with the increase in the current assets, and adding these amounts to the original value in 1901, as computed by the Bureau (which has been considered as the Corporation's investment at that time), the total investment of the Corporation at the close of 1910 may be determined. Such total investment, it is true, may not represent the actual value of the tangible property of the Steel Corporation on that date, particularly on account of appreciation in the value of natural resources, including real estate. The rise in value of property of the Corporation between 1901 and the close of 1910, however, would necessarily have to take account of the great concentration of control of the industry enjoyed by the Steel Corporation particularly with respect to the ownership of ore. This is a factor that cannot be measured here.

Therefore, the Corporation's *investment* in its properties, rather than the *valuation* of these properties, is the proper basis for the current discussion, as well as for computing profits taken up later.

The table on opposite page shows the additions to the investment of the Steel Corporation from 1901 to 1910, together with certain deductions for depreciation which were considered by the Bureau as proper.

The figures of true depreciation given in this table represent the entire estimated depreciation in the properties of the Corporation, including exhaustion and obsolescence. The bulk of such physical depreciation was made good by expenditures on these properties which were not capitalized, thus leaving a

NET ADDITIONS TO INVESTMENT OF STEEL CORPORATION, APRIL 1, 1901, TO DECEMBER 31, 1910

Description	Total Additions	Estimated True Depreciation	Amount Made Good by Expenditures Not Capitalized	Net Outstanding Depreciation to be Deducted from Investment	Net Additions to Investment
Fixed property (exclusive of Gary and Tennessee Coal, Iron and Railroad Company):					
Manufacturing	$151,480,449	$107,060,053	$88,918,509	$18,141,544	$133,338,905
Iron Ore	62,093,931	30,293,497	2,345,016	27,948,481	34,145,450
Coal and coke	34,112,303	21,220,986	5,534,665	15,686,321	18,425,982
Transportation	74,541,029	37,336,955	13,462,331	23,874,624	50,666,405
Miscellaneous fixed property	5,548,556	4,242,626	1,435,982	2,807,544	2,741,012
Other assets:					
Deferred charges	13,243,678	—	—	—	13,243,678
Investments	2,128,364	—	—	—	2,128,364
Sinking funds	16,067,665	—	—	—	16,067,666
Current assets	101,683,544	—	—	—	101,683,544
Total	460,899,520	200,154,117	111,695,603	88,458,514	372,441,006
Gary plant	69,978,695	—	—	—	60,978,695
Tennessee Coal, Iron and R.R. Co.	60,468,518	2,856,003	1,832,843	1,023,160	59,445,358
Add property adjustments	3,063,594	—	—	—	3,063,594
Grand total	594,410,327	203,010,120	113,528,446	89,481,674	504,928,653

balance which may be termed a "net accrued" or "outstanding" physical depreciation not made good, which balance has been set against the additions in order to arrive at the net additions to the investment.

While, therefore, the total allowances for depreciation for certain classes of property appear somewhat excessive, the Bureau, after analysis, has for the purpose of computing the investment accepted these estimates as the actual depreciation

of the Corporation's physical properties. They differ somewhat from the provisional allowances as stated in the annual reports. These provisional allowances in a few cases were admittedly excessive or included amounts not representing actual depreciation. Such excessive provisions have been excluded by the Bureau and also restored to the earnings. The total depreciation allowances given in the table include provisions for blast-furnace relining, which in the annual reports are not included under the provisional depreciation allowances.

The constituent companies of the Corporation very properly compute their depreciation charges (including exhaustion) on the original cost of, or investment in, the various properties and not on the replacement cost (either actually incurred or anticipated).

In addition to the provisions for depreciation above described, the Steel Corporation writes off its property account each year other varying sums, usually of large amount. These further sums, however, as explained by the Corporation to the Bureau, do not represent true depreciation based on original cost or purchase value of the physical property to subsidiary concerns, but are instead an offset of a part of the inflated valuations at which the stocks of the subsidiary companies are carried on the books of the Steel Corporation. Such additional amounts written off by the Steel Corporation itself, on account of overcapitalization, while probably entirely justified from that standpoint, have, however, no relation to the real depreciation of such first cost of the physical properties, and consequently have not been deducted from earnings by the Bureau.

Investment of Steel Corporation at the Close of 1910

The Steel Corporation has made no detailed appraisal of its properties since the close of 1907. The Bureau's computation of the investment in the Corporation's property down to the close of 1910 is given in the table on opposite page.

The Bureau has therefore computed the actual investment of the Steel Corporation in its various properties at the close of 1910 at $1,186,982,038. This compares with a total valuation in April, 1901, of $682,053,385. In other words, during the

INVESTMENT IN TANGIBLE PROPERTY OF STEEL CORPORATION ON DECEMBER 31, 1910, AS COMPUTED BY BUREAU

Description	Investment 1901	Net Additions 1901–1910	Total Investment Dec. 31, 1910
Fixed property (exclusive of Gary and Tennessee Coal, Iron and Railroad Company):			
Manufacturing	$250,000,000	$133,338,905	$383,338,905
Iron Ore	100,000,000	34,145,450	134,145,450
Coal and coke	80,000,000	18,425,982	98,425,982
Transportation	91,500,000	50,666,405	142,166,405
Miscellaneous fixed property	24,000,000	2,741,012	26,741,012
Other assets:			
Deferred charges	2,088,027	13,243,678	15,331,705
Investments	241,030	2,128,364	2,369,394
Sinking funds	239	16,067,666	16,067,905
Current Assets	134,224,089	101,683,544	235,907,633
Total	682,053,385	372,441,006	1,054,494,391
Gary Plant	—	69,978,695	69,978,695
Tennessee Coal, Iron and Railroad Company	—	59,445,358	59,445,358
Adjustments	—	3,063,594	3,063,594
Grand total	682,053,385	504,928,653	1,186,982,038

period from April, 1901, to December 31, 1910, the Corporation has made an additional net investment in its properties of no less than $504,928,653. Of this amount, roughly, $435,000,000 was virtually provided from earnings. These amounts, it should be noted, are over and above the allowance for ordinary maintenance and repairs and for actual net depreciation as given above.

This great addition to the investment of the Steel Corporation has eliminated a considerable amount of the "water" in the original capitalization of the company. The increase in the investment does not, however, exactly measure the amount of water or inflated capitalization thus offset, partly because the capitalization of the Corporation has not been the same. In the first place, the capitalization has been considerably increased, particularly through the issue of new bonds and other forms of indebtedness and also through the assumption of liabilities of several concerns which have been acquired. On the other hand,

a part of this increase has been offset by the liquidation of a part of the bonded indebtedness. Although the preferred stock of the Corporation was reduced in 1903 by $150,000,000, this was accomplished only by a corresponding increase in the bonded debt, by the so-called bond conversion plan, a severely criticized operation and one involving certain objectionable features, fully discussed in the body of the report. The total net outstanding capitalization of the Steel Corporation on December 31, 1910 (including with the capitalization the purchase-money obligations and real-estate mortgages, as in previous instances, but excluding $620,352 par value of stocks of subsidiary companies not held by United States Steel Corporation), was $1,468,033,260. The excess of the capitalization over the indicated investment ($1,186,982,038) was, therefore, $281,051,222, whereas at its organization in 1901 the disparity between the two figures was $720,846,817. It is apparent, therefore, that a large part of the water in the capitalization, as it may be called, has been eliminated.

The Steel Corporation undoubtedly would contend that there was not a disparity of $281,000,000 between its capitalization and the actual value of its property at the close of 1910. Indeed, the Steel Corporation in its balance sheet of December 31, 1910, claimed total assets (after deduction of current liabilities) of approximately $1,693,000,000, or, roughly, $225,000,000 over and above the outstanding capitalization as above stated. Of this excess $164,000,000 was surplus and the balance sundry reserves. This balance sheet valuation, it will be seen, is about $500,000,000 in excess of the investment as computed by the Bureau.

The Steel Corporation in defending its 1910 book valuation undoubtedly would rely in the main upon two considerations — first, that there has been an appreciation in its natural resources, particularly ore, and second, that there is a so-called "merger value" attaching to its properties because of their combination and coördination under a single control.

So far as the ore is concerned, there has been no such marked appreciation as the Steel Corporation claims. Moreover, a considerable part of whatever actual appreciation has occurred in ore values undoubtedly is due to the rapid concentration of ore

property in the hands of a comparatively few interests, and especially in the hands of the Steel Corporation itself.

With respect to "merger value," it is probably true that the various properties acquired by the Steel Corporation, taken together with the organization of this company as a going concern, do have a value in excess of the sum of their values as separate entities. The coördination and integration made possible by the combination of such properties under a single control undoubtedly tend to reduce costs either through economies or through removing the necessity of paying profits to others. Further, in so far as the concentration of the industry under the control of a single concern gives to it a monopolistic power over production and prices, this may result in an increase in its earning power and consequently in an increase in its value as a going concern. This involves, however, the reduction of actual or potential competition. Indeed, much of what is ordinarily termed merger value, in so far as it exists, is to a greater or less degree a monopolistic value. To allow a single company, which has secured the bulk of a given industry, credit for such merger value, as a basis on which to earn profits, raises, therefore, a question of far-reaching public policy. In the absence or ineffectiveness of competition, either actual or potential, earnings might be obtained which, if capitalized at an ordinary rate of profit, would give a value or capitalization greatly in excess of the real investment. To regard a valuation so arrived at as justifying such profits under these conditions would be reasoning in a circle, because the real question is whether the profits themselves, used to determine the capitalization, were reasonable. For the reasonableness of profits, only two criteria are practically available, namely, first, the existence of free and fair competition, and, second, the rate of profit on the actual investment. Of these two criteria the second is the only practicable one available, where competition is not effective. Therefore both because of the vital issue involved, as well as because of the practical consideration of establishing an investment which shall permit of intelligent discussion of profits, the Bureau, while admitting there is an element of merger value in a going concern, either from great concentration of control, monopolistic

power, or other influences, has made no addition therefor to the investment of the Steel Corporation.

Profits of the Steel Corporation

The profits earned upon the investment of the Steel Corporation, as computed by the Bureau, have averaged 12 per cent for the entire period from 1901 to 1910. The extreme range was from 7.6 per cent in 1904 to 15.9 per cent in 1902.

As already stated, the average for the period from April 1, 1901, to December 31, 1910, is 12 per cent. The average rate for the first four and three fourths years was 12.5 per cent, as against 11.6 per cent in the five years from 1906 to 1910. Therefore, in so far as any tendency may be noted, it is toward a lower rate of profit in recent years.

The table shows that in the years 1904 and 1908, which were years of rather marked depression in the iron and steel business, the rate of profit of the Steel Corporation fell to 7.6 per cent on the investment in 1904 and 7.8 per cent in 1908, as compared with a maximum profit of over 15 per cent in 1902 and 1906. Prior to the formation of the Steel Corporation and other large consolidations, the iron and steel industry was noted for violent changes in the rate of profit, the industry, indeed, having been aptly termed either "prince or pauper." This table shows that so far as the Steel Corporation is concerned the business, although still subject to marked fluctuations in profits, has, even in the most depressed years of this period, shown a substantial return on the actual investment.

It should be pointed out that an average rate of 12 per cent for a concern of the size of the Steel Corporation, which embraces more than one half of the entire iron and steel industry of the country, has a very different significance than the same rate in the case of a relatively small concern. While exceptionally efficient or fortunate concerns in the steel business may earn rates in excess of this average, on the other hand a great many of the less efficient companies undoubtedly earn very much smaller rates, while in some instances the business is conducted at a loss. Therefore, an average rate of 12 per cent for over

one half of the entire steel business of the country is so much more significant than the same rate or even a larger rate for a comparatively small concern. It probably means that the return on a considerable proportion of the business of the country, which under more competitive conditions and more scattered ownership would be conducted at a lower rate of profit, has been considerably increased.

It may also be noted that the investment includes a large amount of idle property, particularly unimproved ore reserves, which, of course, tends to reduce the rate. However, the investment in undeveloped iron-ore property as computed by the Bureau is not so great as to very materially affect the rate of profit. Nevertheless it is worth emphasizing that the rate of profit here given includes not only the iron and steel industry proper, but also the iron-ore mining industry. Prior to the era of consolidation the latter, to a large extent, was distinct from the manufacture of iron and steel, and under the scattered ownership of iron-mining properties then prevailing profits generally are understood to have been comparatively low, on the average. Under present conditions in the iron and steel industry, however, the Lake iron-ore industry is one of the most profitable branches of the business. This factor should be considered, therefore, in comparing the profits of the iron industry at the present time with those obtained under the different conditions formerly prevailing.

The rate of earnings on the investment of the Steel Corporation as computed by the Bureau is, of course, considerably larger than the rate of net profit upon the capitalization, as indicated by the annual reports of the Corporation, because the investment as established by the Bureau is very much less than the capitalization. The rate of 12 per cent here given, it should be clearly understood, covers the entire investment in the property, whether represented by capital stock or bonded debt. This rate of earnings on the total true investment understates the rate which accrues to the benefit of the Steel Corporation (or the stockholders as distinguished from the stockholders and bondholders combined) on that part of the true investment which may be considered as represented by the capital stock. That is

to say, if that part of the true investment for which bonds were issued were deducted from the total true investment, and a corresponding amount of bond interest at the rates paid by the Corporation were deducted from the earnings, then a comparison of the remainder of the investment with the remainder of the earnings would indicate a considerably higher average profit than 12 per cent. Such a computation, however, cannot be made in a definite or satisfactory manner, particularly because the original bonds issues of the Corporation did not correspond with the true value of the property for which they were issued. Therefore, to deduct them from the true investment would leave an unduly low remainder for the capital stock and unfairly exaggerate the rate of profit on that part of the true investment which may be considered as being contributed by the stockholders.

Hence the Bureau does not attempt to give in definite figures the rate of profit earned by the Steel Corporation on the true investment represented by its capital stock, but merely calls attention to the fact that the rate of profit above shown is not the rate earned on that part of the true investment which may be considered as contributed by the stockholders, but a lower rate earned on the total true investment and accruing to the stockholders and bondholders combined.

Position of Steel Corporation in the Industry

The Steel Corporation, despite its great size, is not exempt from competition. Indeed, the evidence on the whole indicates that competition in the industry has steadily been increasing. Notwithstanding the great additions made by the Corporation to its properties from earnings and the acquisition of several important competing concerns, its proportion of the business in nearly every important product except pig iron and steel rails is less than it was in 1901. This is shown by the table on opposite page of percentages compiled by the Corporation from its own figures in connection with data gathered by the American Iron and Steel Association.

The Steel Corporation did not compute its percentage of the ore production of the country. Its proportion of the production

PROPORTIONS OF OUTPUT OF PRINCIPAL IRON AND STEEL PRODUCTS PRODUCED BY UNITED STATES STEEL CORPORATION AND BY INDEPENDENT COMPANIES, RESPECTIVELY, IN 1901 AND 1910

PRODUCTS	STEEL CORPORATION'S PERCENTAGES		INDEPENDENT COMPANIES. PERCENTAGES	
	1901	1910	1901	1910
Pig iron, spiegel, and ferro	43.2	43.4	56.8	56.6
Steel ingots and castings	65.7	54.3	34.3	45.7
Rails	59.8	58.9	40.2	41.1
Structural shapes	62.2	[3] 47.0	37.8	[3] 53.0
Plates and sheets of all kinds [1]	64.6	[3] 49.7	35.4	[3] 50.3
Black plate produced in tin mills	79.8	52.9	20.2	47.1
Coated tin-mill products	73.1	61.1	26.9	38.9
Black and coated sheets produced in sheet mills	67.3	38.9	32.7	61.1
Wire rods	67.7	67.3	22.3	32.7
Wire nails	68.1	55.5	31.9	44.5
Wrought pipes and tubes [2]	57.2	38.2	42.8	61.8
Seamless tubes [2]	82.8	55.3	17.2	44.7

of Lake Superior ore, such ore being practically the basis of the steel industry (arrived at by comparing the known production of the Steel Corporation with the total production as estimated by the Geological Survey), fell from 60.6 per cent in 1901 to 51.6 per cent in 1909 (figures for 1910 not being available).

This table shows that whereas the Steel Corporation in 1910 had fully maintained the share of the country's total production of pig iron which it held in 1901, its proportions of the production of nearly all steel products had declined, and in most cases sharply declined. The only important exception was steel rails. The maintenance of its proportion here is chiefly due to the erection of a very large rail mill at the new Gary plant and to the acquisition of the Tennessee Coal, Iron and Railroad Company, which had a considerable steel rail production.

[1] Includes sheets for tinning, galvanizing, and other coatings.

[2] These percentages are based on capacity and not production. The capacity of independent companies is, moreover, partly estimated.

[3] For 1909; figures for 1910 not available.

Taking the production of steel ingots and castings as a basis it will be seen that the Steel Corporation's percentage of the total fell from 65.7 per cent in 1901 to 54.3 per cent in 1910. This figure, perhaps, is the best single criterion by which to judge the change in the Corporation's position in the steel industry from a producing standpoint. It will be seen that the Corporation's proportions of production of black plate, coated tin-mill products, and black and coated sheets, fell off to a very marked extent, which indicates that competition has been particularly active in these branches. Its share of the production of wrought pipe and tubes and of seamless tubes likewise fell off very heavily. In wire products the Corporation has maintained its relative position rather better, but even in these there has been a marked recession in the percentages of the business done.

It should be noted that the decline in the production shown by this comparison of the 1901 and 1910 percentages was practically continuous for most products throughout the entire period. However, the actual output of the Corporation has shown a very great increase. For example, the Steel Corporation's production of crude steel ingots, which is typical of its total business, increased from 9,743,918 tons in 1902 (the first full year of operations) to 14,179,369 tons in 1910, an increase of 45.5 per cent.

While, however, these statistics clearly show the existence of active competition in production, it should be clearly pointed out that such competition has not been so evident with respect to prices, where it has been materially modified by the existence of a price policy described as "coöperation." This will be discussed in a later part of the report.

While the Corporation's proportion of the production of both raw materials and finished products thus shows a marked decrease, the proportions given do not fairly represent the true position of the Corporation in the industry as a whole. In iron ore, in particular, the Steel Corporation undoubtedly occupies a dominating position. The Corporation's holdings of what are now regarded as commercially available ores exceed those of all other iron and steel interests combined. It should be clearly understood that the ores of the Lake Superior region substan-

tially form the basis of the steel production of the country at the present time. While the Steel Corporation has very extensive holdings of ore elsewhere, the great bulk of its ore holdings are in the Lake Superior district. In 1907 the holdings of the Steel Corporation in Minnesota, which state includes the Mesabi and Vermilion ranges, according to a carefully prepared schedule of the Minnesota Tax Commission, amounted to about 913,000,000 tons, or 76 per cent of the total ore deposits for the state.

The Corporation's proportion for the whole Lake Superior region, including the old ranges in Michigan, is apparently about the same. Authoritative data submitted to the Senate Finance Committee in 1909 by a prominent iron manufacturer with the Steel Corporation's consent showed that the Corporation itself then reckoned on about 1,625,000,000 tons of Lake ore, of which 1,258,000,000 tons was of the current commercial standard. An estimate of a prominent mining engineer, submitted to the Finance Committee at the same time, placed the total reserves of Lake ore of the commercial standard at about 1,600,000,000 tons. On this basis, therefore, the Steel Corporation would have had over 75 per cent of the total commercially available ore in the entire Lake Superior region. Of course, the ideas of the consulting engineer and those of the Steel Corporation's experts as to what were commercially available ores may have differed somewhat, but it is not likely that the proportion of ore controlled by the Steel Corporation as shown by these two estimates is too high, because both of these statements were submitted by the manufacturer in question together with extensive data for other ore supplies in the United States for the avowed purpose of proving that the proportion of the ore supply controlled by the Steel Corporation was less than 85 per cent of the total supply. In 1908 the commercially available ore of the Lake Superior region, as computed by the United States Geological Survey, for the Conservation Commission, was 3,500,000,000 tons, but the iron content assumed as a basis for available ore was considerably lower than in the two preceding estimates, thus greatly increasing the total quantity. This and other evidence indicates that the Survey estimate is not fairly comparable with that of the Corporation.

In this connection it may be stated that the chairman of the Steel Corporation, in his testimony before the Ways and Means Committee in 1908, admitted that the Corporation had control of the ultimate ore supply of the whole country. Later, however, in 1911, in testimony before a special committee of the House of Representatives, he materially modified that statement.

In discussing the Corporation's position in the ore industry account must be taken of the fact that new discoveries of ore are constantly being made, and also that when somewhat lower grades of ore become commercially available the total reserve will be greatly increased. The use of ore of much lower grade involves, however, much higher costs of production, so that any concern which has substantial control of the best grades of ore would under such circumstances be in a position to obtain an enormous increase in profits. Taking conditions as they are to-day, there can be no doubt that the Steel Corporation has control of the great bulk of the commercially available ores of the Lake Superior district, its proportion probably being about three fourths of the total. In addition, of course, it has there a large amount of low-grade ore, as well as immense deposits in the South. The Corporation's total ore holdings may be conservatively placed at more than 2,500,000,000 tons.

The system of leasing ore mines, as employed in the Lake region, is important in this connection. A very large part (approximately two thirds in 1910) of the Corporation's total holdings in the Lake region is held by lease. Frequently there is no initial investment in such leaseholds, and even where a bonus is paid it is usually small, while the minimum tonnage on which royalty must be paid, whether mining operations are conducted or not, is generally unimportant. The Hill lease is, of course, as above shown, a very marked exception in the last respect.

It will be seen, therefore, that this ore-leasing system, where there is no limit placed on the number of leases that can be combined under a single interest, greatly facilitates the gathering in by a great concern like the Steel Corporation of a vast amount of ore reserves, far in advance of any commercial need for them. This not only prevents others from getting such property but also secures to such a concern the benefit of any appreciation

in value which may come about either from natural causes or as a result of this very concentration of ownership. Obviously, a system which thus lends itself to such marked concentration of ore property for many years in advance (a common term of lease being fifty years), at a comparatively small cost, involves questions of the highest public importance. It might be said that the lease system as thus applied in the Lake ore region really affords an opportunity for a wealthy interest to attempt a corner tin ore reserves on what is, in effect, a margin basis. Of course in such extensive acquisitions there is a decided speculative risk, just as in similar efforts to control commodity markets, particularly, the possibility of the discovery of available deposits elsewhere, or new methods of mining which may render what are now nonavailable ores available for present commercial purposes.

The dominating position in the ore industry enjoyed by the Steel Corporation through this great ownership of ore reserves is heightened because of its very marked degree of control of the transportation of ore in the Lake Superior district. The Corporation owns two of the most important ore railroads, the Duluth and Iron Range Railroad and the Duluth, Missabe and Northern Railway. The ore rates on these railroads are about 1 cent per ton mile. Their operating expenses are very low, that of the Duluth, Missabe and Northern in 1910 being below 30 per cent of gross earnings as against an average of 66 per cent for all the railroads of the country. The net earnings of these ore railroads, which are chiefly from the ore traffic, are phenomenal. This has the practical effect of reducing the Steel Corporation's net cost of ore to itself at upper Lake ports and, on the other hand, of increasing that cost to such of its competitors as are dependent upon the Corporation's railroads for transportation.

Hence, not only on account of its great holdings of ore but also on account of these peculiar advantages enjoyed in the transportation of the ore the Steel Corporation occupies an extremely commanding position in the iron and steel industry. Indeed, in so far as the Steel Corporation's position in the entire iron and steel industry is of monopolistic character it is chiefly through its control of ore holdings and the transportation of ore.

VII

THE UNITED STATES STEEL CORPORATION'S BOND CONVERSION[1]

ON April 17, 1902, the president of the United States Steel Corporation issued a circular to the stockholders, which invited their coöperation in a plan to raise $50,000,000 of new capital. Half of this amount was to repay loans incurred by the constituent companies for construction work which was in part rendered unnecessary by the merger, but which, owing to advance commitments, could not be suspended. In addition, $25,000,000 was required for improvements, which, it was stated, would effect an annual saving of at least $10,000,000. The plan proposed to the stockholders for raising this money was "to rearrange your corporation's capitalization (which, in round numbers, now consists of $300,000,000 of bonds, $500,000,000 of preferred stock, and $500,000,000 of common stock) by substituting for $200,000,000 of the preferred stock, $200,000,000 of sinking fund sixty year 5 per cent mortgage gold bonds, and by selling $50,000,000 of additional bonds of such issue for cash. As the preferred stock carries 7 per cent dividends, while the bonds would bear but 5 per cent interest, the $50,000,000 desired could, in this way, be added to the corporate resources, and the aggregate of the annual charges for interest and dividends, instead of being increased $3,500,000, would be decreased $1,500,000 as compared with the present sum total of these two requirements."

The plan offered to each preferred stockholder the right to subscribe to the new bonds to the extent of one half his holdings of preferred stock, 40 per cent of each subscription to be

[1] From the *Quarterly Journal of Economics*, Vol. XVIII, 1903, pp. 22–53, with certain minor editorial emendations approved by the author. The genesis of the Steel Corporation is outlined in Chapters V and VI, *supra*.

payable in preferred stock, and 10 per cent in cash, or the subscription could be limited to 40 per cent, in which event no cash payment was required. The circular also stated that a syndicate had been formed, "including some directors," to further the success of the plan; and, in the call for a special meeting of stockholders to be held May 19, one of the purposes of the meeting was stated to be the ratification of an agreement between the United States Steel Corporation and J. P. Morgan and Company, acting for this syndicate.

This agreement is dated April 1, 1902, and contains the following provisions:

1. That the party of the second part, known as "the bankers," on or before the first day of July, 1902, should offer to the preferred stockholders the right to subscribe to the second mortgage bonds of the company, on the terms mentioned in the circular, for a period of thirty days;

2. That such part of the $250,000,000 of bonds as should not be taken by the preferred stockholders, should be issued to the bankers on their request for the syndicate, to be paid for in preferred stock, and in cash, on the same terms as those offered to the preferred stockholders, in such amounts and at such times as the bankers might request, up to October 1, 1903;

3. That the bankers guarantee to the Steel Corporation that subscriptions to the new bonds to the amount of $100,000,000 would be made, payable $20,000,000 in cash, and $80,000,000 in preferred stock;

4. That, as compensation for the risk, the guarantee, and the various obligations assumed by the syndicate, the Steel Corporation should pay to the bankers a cash compensation equal to 4 per cent upon the aggregate amount of the bonds which should be sold or delivered, either to the preferred stockholders or to the syndicate, until October 1, 1903.

The plan and the syndicate agreement were submitted to the stockholders, and both were approved by a vote of 7,704,288 shares to 12,540 shares out of a total number of 10,185, 811 shares outstanding.

Before the plan could be put into effect, an injunction was applied for on June 8, 1902, before the Chancellor of New

Jersey, against J. P. Morgan & Co. by Miriam Berger, a preferred stockholder, to forbid them to issue bonds for stock under the bankers' contract, and alleging that the plan of conversion was unlawful for the following reasons: (1) that the plan, if carried out, would impair the complainant's vested rights as a stockholder; (2) that the plan of issuing bonds to retire stock was void against any dissenting stockholder; (3) that the plan was ruinous and disastrous, and impaired the value of complainant's stock; (4) that four members of the bankers' firm were directors of the corporation; and (5) that the compensation which might be received by the bankers under their contract was without consideration and illegal, and that the scheme was devised to secure exorbitant commissions by this firm. An order restraining the bankers from issuing any bonds in exchange for preferred stock was granted by Vice-Chancellor Emery on the ground that the complainant's vested rights would be impaired by the exchange of bonds for preferred stock under the terms proposed.[1] The case was appealed, the appeal being argued on June 25.

Before the appeal was decided, on July 5, a second bill was filed by J. Aspinwall Hodge, Bernard Smith, and William H. Curtis against the corporation, the bankers, and the directors.[2] The grounds on which relief was asked for were as follows:

1. That the plan interfered with the vested rights of the complainants;

2. That it was *ultra vires* and void;

3. That the Steel Corporation, under the act of 1902, could not issue bonds for stock, because it had not paid dividends on the preferred stock for at least a year preceding the date of the

[1] The ground on which the injunction was granted was: "that it (the conversion plan) is a preferential distribution of capital among some of the shareholders to the exclusion of others, and not a plan for an equal distribution among all the preferred stockholders. That the capital represented by preferred stock up to a limit of $200,000,000 is to be reduced to the extent the holders agree to take bonds, and . . . the stock of those who decline to take bonds is thus made subject to the prior claim and lien of those who take bonds."

[2] Smith and Curtis, it being proven that they were not registered owners of stock at the time suit was brought, obtained no recognition in the litigation. The right of Hodge to petition for an injunction was recognized.

meeting, and because its assets, after deducting the amount of its bonded debt, were not equal in value to the par value of its preferred stock;

4. That the scheme was disadvantageous, and would seriously damage the corporation and its stockholders, and that the compensation to the bankers was exorbitant;

5. That the action of the directors in approving the plan and contract was void, because fifteen or more of the board of directors were interested in the underwriting syndicate;

6. That the plan was never legally ratified by the necessary two-thirds vote of the stockholders, because the votes upon the stock controlled by the bankers and members of the syndicate must be counted to make up the two-thirds vote required by law.

The injunction asked for was granted October 29, 1902, on a portion of the third item of the bill of complaint, on the ground that only four continuous payments of dividends on the preferred stock had been made, the duration of the period from the time of the first declaration of a dividend, July 2, 1901, to the date of the stockholders' special meeting, May 19, 1902, being forty-four days less than one year, while five continuous quarterly payments should have been made to fulfil the requirements of the law. An appeal was allowed to the Court of Errors and Appeals, where the case was re-argued in the November term. Decision was rendered on February 18, 1903, reversing the Vice-Chancellor, and deciding in favor of the defendants, on the ground that all the requirements of the law had been complied with, and that "there is no ground presented by the case or agitated in the briefs of counsel which will justify the interposition of a court of equity to arrest the proposed action of the defendants." A similar decision had been rendered by the Court of Appeals in the Berger case on October 11, 1902. The Steel Corporation at once put its plan into effect.

It is proposed, in the following pages, to outline the principal arguments in the Hodge suit as found in the affidavits, briefs, and arguments of counsel. Space does not, however, permit an extended analysis of these arguments; and, for the most part, the merits of the controversy will be determined by the decisions of the Vice-Chancellor and the Court of Appeals upon the dif-

ferent points presented. The complainants in the Hodge suit presented the most varied and forcible criticisms which have been made of the bond conversion plan. It may also be presumed that the defendants placed their side of the question in the most favorable light. With the opinions of two courts to assist him, the reader will have little difficulty in determining on which side lay the weight of the evidence.

Omitting the claim that the vested interests of the complaining stockholders would be impaired by the proposed conversion of preferred stock into bonds,—this point being decided in the Berger suit in favor of the corporation,[1]—and passing over, as being of merely technical interest, the ground on which the Vice-Chancellor granted the injunction, we find that the complainants rested their case upon the following principal arguments:

1. That the action of the directors in sanctioning the plan was illegal, by reason of the private interest of several of their number, while the stockholders, to whom the extent of the directors' interest had not been fully disclosed, could not validate their illegal action;

2. That the scheme was vitiated by actual fraud, being plainly designed to favor J. P. Morgan & Co. and their associates, at the expense of the corporation;

3. That the contract with the syndicate was unfair to the stockholders, both in the length of time given to them to subscribe for the bonds as compared with the time allotted to the syndicate, and the unreasonable options granted to the bankers;

4. That the Steel Corporation did not have assets of the value required by law.

In developing the alleged illegal private interest of the directors, the complainants began by claiming that fifteen of the directors of the Steel Corporation, including the six members of

[1] Opinion of the Court of Errors and Appeals, Van Syckel, J., (p. 11): "That this plan involves a reduction of capital stock is conceded: it is the very purpose of the plan to reduce it and to retire it; but to the assertion that it is preferential, I am unable to assent. The same opportunity is given to all to accept the offer, none are excluded, and the complainant who has declined the offer cannot say to the ninety and nine who have accepted it that they have been preferred. There has been no preference on the part of the corporation; the position occupied by the complainant is of her own option."

the Finance committee, were members of the underwriting syndicate whose agreement with the syndicate managers was dated March 12, twenty-eight days before the resolution of the directors approving the contract between the syndicate and the Steel Corporation. In other words, at the meeting on April 1, when the contract with the syndicate came up before the directors, a majority of the board were "personally and individually interested in the profits and advantages to be derived by Morgan & Co. and their associates." . . .

These benefits were considerable. If the stockholders subscribed to the full amount of $250,000,000 of bonds, the syndicate would receive $10,000,000 in cash from the corporation. In addition to this large commission, the syndicate had the privilege of exchanging preferred stock for all bonds which were not taken by the stockholders; and this option, it was claimed, presented the certainty of a large additional profit. It is the law of New Jersey that where the personal interest of a director is concerned in a contract with his corporation, that contract is voidable. On this ground, the complaints asserted that the action of the directors was illegal.

The answer to this argument, reserving to a later page a discussion of the benefits of the contract, was short and decisive. Such contracts as the one in question, said the defendants, while voidable at the option of the stockholders, can be validated either expressly by a vote of the stockholders, or by the stockholders not electing to take any action in the matter. In the present instance, since the stockholders, by an enormous majority, had sustained the directors in their approval of the plan of conversion, to say nothing of the fact that the by-laws of the corporation expressly provided that directors might be interested in contracts with the corporation, and, further, "that . . . any act or contract that shall be approved or ratified by the vote of the holders of a majority of the capital stock of the company . . . shall be as valid and binding upon the corporation and upon all the stockholders as though it had been approved or ratified by every stockholder of the corporation," the court held that the infirmity in the contract had been entirely eliminated, and that the ratification of the agreement and plan was complete.

The complainants then attempted to show that less than the necessary amount of stock was legally voted, by setting up the plea that the members of the syndicate had no right to vote for the ratification of a scheme in which they were personally interested as opposed to the interest of the corporation, thus affirming the doctrine that the rights of a stockholder, when he becomes a director, are limited by the director's obligation to the corporation, which, it was alleged, was violated in the present instance, and going so far as to impose a similar obligation upon a stockholder who was not a director. This argument was stated as follows: . . . "It is contended that where a large number of stockholders conspire to impose a burden upon a corporation for their own benefit, ignoring the interest of the corporation, they thereby become constructively trustees for their fellow-stockholders, assume the obligations of trustees toward their fellow-stockholders, and must deal with them accordingly."

The defendants replied, and the court agreed with them, that a stockholder can never be deprived of his right of ownership in a corporation and of the right to vote the number of shares which he holds upon any question affecting his interest. Judge Van Syckel remarked in his opinion:

They [the directors] voted upon that resolution, not as directors, not in their fiduciary capacity, but solely in the right of the shares of stock held by them. A most valuable privilege, which attaches to the ownership of stock in a corporation, is the right to vote upon it at any meeting of stockholders. As to the resolution considered by itself, as stockholders, they owed no greater duty to their co-stockholders than those stockholders owed to them. Like other stockholders, they had a right to be influenced by what they conceived to be for their own interest, and they cannot lawfully be denied that right, nor can it be limited or circumscribed by the fact that they occupied the position of directors in the company.

But, continued the complainants, granted that the vote was legal on the assumption that the stockholders fully understood the nature of the resolutions upon which they were voting, that assumption was contrary to the facts. The stockholders were not aware of the nature of the contract already made with the syndicate, nor with the extent of the personal interest of the

directors in this contract. The only information in regard to these matters contained in any of the documents sent to the stockholders, appears in the circular of April 17, and was as follows: "To further the success of the plan, there has been formed a syndicate, including some directors, which will receive four-fifths of the 4 per cent compensation to be paid under the contract with Messrs. J. P. Morgan & Co. mentioned in the notice of stockholders' meeting." It was further stated in the notice of the stockholders' special meeting, that copies of the directors' resolution, in which the nature of the contract was explained, and of the contract itself, could be obtained on application at Morgan & Co.'s office. This notice, the complainants asserted, was insufficient to acquaint the stockholders with the nature of these contracts which they were asked to approve.

The defendants replied in the words of a decision upon another case cited in the brief of the defendants upon appeal:

> If the party notified make reasonable investigation, he obtains actual knowledge of these facts; if he choose not to make it, he is charged constructively with knowledge of them. . . . If he is unwilling to act upon the facts as the notice presents them, then the law demands that he shall make proper examination, and upon the result of that examination he may safely stand. . . . But, if he prefer not to examine, it must be because he is satisfied to act as if the matters disclosed in the notice were true, and he cannot afterward complain if his rights are made to rest upon them so far as they are true. The information given by the notice is equivalent to that obtained by the inquiry.[1]

This principle has been established in a number of cases. It was reaffirmed by the Court of Appeals in its decision that the information furnished to the stockholders of the Steel Corporation in regard to the various contracts and resolutions was sufficient to put them on inquiry. In fact, so little question was raised at the time concerning the expediency of the scheme that no stockholder applied to J. P. Morgan & Co. for a copy of the contract. The defendants were, therefore, apparently justified in their claim that the stockholders received all the information which they required.

[1] *Gale* v. *Morris*, 3 Stew. 285, 289, 290.

The Charge of Fraud

The evidence submitted by the complaining stockholders to substantiate their charge of fraud lay in the nature of the transactions in controversy. They claimed that the conversion scheme was bound up with the syndicate agreement; that it would not have been brought forward had it not been for the benefits which the syndicate was to derive; and that the compensation received by the syndicate, and the privileges allotted to it, were unreasonable and extortionate.

Here was a corporation, they said, in urgent need of at least $50,000,000 to complete improvements already begun, and to undertake further improvements whose completion would add at least $10,000,000 to its profits. This money was to be borrowed on the security of a second mortgage. The interest was to be provided by converting a 7 per cent dividend charge on $200,000,000 of preferred stock into a 5 per cent interest charge on the same amount of bonds. Ostensibly to insure the success of this plan, the aim and object of which was to raise a certain amount of cash, an underwriting scheme was devised, which, however, entirely subordinated the raising of cash to the conversion of stock into bonds. The underwriting plan devised by the directors undertook to guarantee, not the amount of cash required, but a plan of conversion whose complete success would not have increased the security of the proposed bond issue, nor have rendered the bonds more attractive in the eyes of investors, — a measure, moreover, which made inadequate provision for the real needs of the corporation. The syndicate, in other words, instead of guaranteeing to take $50,000,000 of bonds at par, and to pay for these bonds in cash, which the commonly understood principles of underwriting demanded, agreed to take only $20,000,000 of bonds at par, for which, after deducting their assured commission of $4,000,000 on the $100,000,000 of bonds whose purchase with cash and stock they had guaranteed, the corporation would receive only $16,000,000 of cash. Moreover, if the amount of bonds remaining should be taken by the stockholders, the additional commissions of the syndicate would reduce their actual cash guarantee

to $11,200,000, or little more than one-fifth of the amount which the stockholders have been told was necessary. On the basis of the actual cash furnished, the commission to the syndicate, assuming that the plan was successfully carried out, would be 44 per cent, — an extraordinary and unreasonable compensation.[1]

Furthermore, in answer to the argument set forth in the affidavit of Mr. Perkins, in which he claimed that, in the opinion of the Finance Committee of the Steel Corporation, the immediate effect of the announcement of the contemplated withdrawal of 40 per cent of the preferred stock would be to send its price above par, and so make conversion unattractive, and that the necessity of segregating a large amount of preferred stock in order to make sure that at least $80,000,000 of stock would be exchanged, as provided by the syndicate agreement, involved great risk and the locking up of a large sum of money for a considerable time, the complainants urged that, in any event, the bonds, which were, on the admission of the Finance Committee of the Steel Corporation, a higher grade security than the preferred stock, — else why convert the stock into bonds? — would always sell at a higher price than the stock, and that, therefore, the necessity of guaranteeing the conversion did not appear. There could be no reasonable doubt that the corporation could sell $20,000,000 of its second mortgage bonds for more than $16,000,000, the maximum amount of cash which it stood to receive from the syndicate. The assurance given by the syndicate that the amount required for distribution to the security holders would be decreased $1,500,000 per year could have no effect upon the price of the bonds, and could therefore lend only indirect assistance to the conversion. Moreover, a large amount of this $80,000,000 preferred stock was already the syndicate's property at the time the contract was made; and, so far from locking up funds in fulfilling their agreement, the members of the syndicate were in reality increasing the value of their property. In short, it was claimed that the guarantee of the syndicate contained an inconsiderable benefit for the Steel Corporation, in return for which the syndicate was to receive a large cash commission.

[1] Argument of Edward B. Whitney for Appellees, p. 21.

The Charge of Discrimination

In support of the charge of discrimination, the complainants argued that the plan created two classes of subscribers to the new bonds: (1) the syndicate; (2) the other preferred stockholders. Class 1 were offered the bonds at 96; class 2, at 100. Class 1 had an option on part of the bonds for seven and one-half months, and an option on such portion of the remainder as were not taken by the preferred stockholders for sixteen and one-half months, which period could be extended by agreement between the syndicate and the directors. Class 2 had an option limited to fifty-eight days. Class 1 could exchange their holdings of preferred stock to any amount, while class 2 were limited to 40 per cent of their preferred stock holdings. "The syndicate," said the complainants, "after cutting off the preferred stockholders not in the syndicate by the thirty (or fifty-eight) days' notice, could, at any time before the first day of January, 1904 (and later by means of extending the time), purchase 1000 shares of preferred stock at the market price, — say 83, — paying therefor $83,000; then call upon the Steel Corporation under one of the options to deliver to them bonds to the amount of $100,000 in exchange for the 1000 shares of stock, and sell the bonds at the market price, — say 95, — thus making $12,000 without the slightest trouble or expense, except that which would attend a few minutes' clerical work. And this process could be repeated in larger or smaller amounts from time to time, whenever the relative market prices of the stock and bonds should make it profitable to do so. Would not this be a palpable injustice to stockholders of the corporation, and especially to the preferred stockholders, not members of the syndicate, who had exchanged 40 per cent of their preferred stock for bonds?"

The answer of Mr. Perkins to this charge has been already referred to. He asserted that, without the guarantee of the syndicate, the success of the conversion plan would have been endangered by the appreciation in the value of the preferred stock. He does not answer the argument that the compensation was excessive in consideration of the benefit received by the corporation, except so far as to assert that the syndicate

agreement was "a most desirable one for the United States Steel Corporation," but rests the justification of the compensation almost entirely on the risk assumed by the syndicate.[1] In the Berger suit, where this point was more fully discussed, and to which constant reference was made in the Hodge litigation, the expediency of the contract with the syndicate was justified by the argument which Mr. Perkins employed, and the large risk incurred by the syndicate was thus explained in the brief of counsel for the corporation:

Is it reasonable to contend that the tying up of $100,000,000 of capital involves no risk or consideration and warrants no compensation? Can it be said that a syndicate, which undertakes an obligation of $100,000,000 and for the purpose of performing that obligation ties up by actual deposit $80,000,000 of property, is furnishing no consideration for an agreement to pay a commission? Suppose, pending action by the stockholders, the preferred stock of the syndicate had fallen in value from 94 to 87½ (as it actually did) or even lower, and there was a falling market occasioned by strikes or financial disaster, who would recompense the syndicate for the loss that it would sustain by the depreciation of its stock? . . . A variation of four points in the relative value of the seven per cent cumulative preferred stock and the new five per cent bonds would at once wipe out the profits of the syndicate and turn the venture into a loss. . . . For example, it may well be that the present market value of the proposed new five per cent bonds is 95, and that the present market value of the preferred stock is 88, a depreciation of 6 per cent since the syndicate deposited the $80,000,000 of stock. What, then, would be the outcome of the risk of the syndicate if the plan had been disapproved by the stockholders, or if it should now be set aside by the courts? The syndicate has tied up $80,000,000 of stock, which now shows a loss of 6 per cent, or $4,800,000, and this loss exceeds the promised commission, which they would not receive if the contract were not approved, and in addition the syndicate is

[1] The following quotation from Mr. Perkins's affidavit is of interest in this connection: "The largest participations in the syndicate were taken only after urgent solicitation by me and upon my agreeing that my firm would take an equal amount. The participation taken by Mr. Schwab and by some of the other directors was upon the understanding that, if we found other parties to take any part of such participations, we would do this, and thus release them. My firm considered, and I believe most of the directors believed, that the syndicate contract was not a particularly profitable one for the syndicate. In no instance did we find any stockholder willing to subscribe for the full amount of his holdings in preferred stock."

bound to take $20,000,000 of bonds, which bonds are only worth 95 in the market, showing an additional loss of $1,000,000. It is submitted that the mere statement of these facts must satisfy any court that the syndicate has since the first of April, 1902, run a very great risk, that it is still running a great risk, that in all fairness and propriety a reasonable compensation may be paid for that risk, and that the agreed compensation is not excessive.[1]

It is unfortunate that the defendants did not feel themselves compelled to legitimate the syndicate agreement, not merely by citing the risk undergone, but, as the complainants challenged them to do, by showing a corresponding benefit to the corporation. As complainants' counsel remarked:

The directors of an industrial corporation would not be justified in paying a million dollars to a person who offered to swim the Atlantic. unless they could show that some benefit would be conferred upon the corporation by the accomplishment of that feat. The fact that the gentleman proposing the scheme insisted upon the enormous risk that he ran would not justify the directors in closing the contract.

It would have been better, we must admit, if only for the sake of gaining a larger measure of general approval for their project, if the defendants had presented this portion of their argument in a less general and sweeping manner.

For the immediate purpose of winning their case, however, it was merely necessary for the defendants to keep before the court the fact that the contract between the Steel Corporation and Messrs. J. P. Morgan & Co. was approved of by more than 99⅘ per cent of the stockholders represented at the special meeting. Behind this fact, in passing upon the legitimacy of the transaction, in the absence of specific proof of fraud, the court could not go. As Vice-Chancellor Emery said in his opinion which was quoted in the decision of the appellate court:

The reasonableness or judiciousness, in the business aspect, of a reduction of the preferred stock of the Steel Corporation, and the distribution of capital resulting therefrom, by the conversion of stock into bonds, is . . . altogether a matter of management of the affairs

[1] Brief on Behalf of Defendants — appellants in *Miriam Berger* v. *United States Steel Corporation*, pp. 42, 43, 44.

of the corporation, upon which the decision of the directors and stockholders given in the manner required by law is final, so far as it relates to its business aspects.

And Judge Van Syckel, in the final decision, stated the same principle in more general terms, quoting from his opinion in the Berger case:

The manner in which a duly authorized plan is to be carried through is part of the business of the corporation, and, in the absence of fraud or bad faith, is not the subject of judicial control to any greater extent than any other business of the corporation. The court cannot substitute its judgment for that of the directors and majority stockholders, and say that a less expensive plan could be successfully adopted.

In short, so long as the directors acted in good faith and with entire frankness, they might, unless expressly forbidden by the law, have converted all their preferred stock into a 6 or 7 per cent bond; they might have incurred a floating debt equal to their mortgage indebtedness; they might have abolished the charge for depreciation; they might have paid their president a salary of $5,000,000 per year. In fact, they might have violated many rules of business prudence if only they could secure the approval of a majority of the stockholders. In New Jersey, a stockholder, generally speaking, is allowed to do what he will with his own.

That the court was convinced of the honesty and good faith of the transaction appears from the expression of Justice Van Syckel:

There is an entire absence in the case of anything to show a taint of fraud, or an attempt to conceal from the shareholders any fact which should have influenced their action. That the entire proceeding was conducted with good faith, without concealment, and with fairness to both parties, is evinced by the fact that during all the litigation which has ensued, under the promotion of a shareholder who did not attend the meeting, not one of the vast number of shareholders who were present in person or by proxy, comprising men of great business capacity, interested to the extent of millions of dollars in the conversion plan, has questioned its propriety, or expressed a desire, so far as appears, to recede from it.

The Valuation of the Assets

A New Jersey corporation cannot convert preferred stock into bonds unless its assets, after the deduction of all indebtedness, are equal to its preferred stock.[1] In their attempt to prevent the conversion of preferred stock into bonds, the complaining stockholders laid final emphasis upon the alleged fact that the assets of the Steel Corporation were not worth the necessary amount; namely, $880,024,900. In proof of this assertion, the complainants relied mainly upon the affidavits of one James H. Lancaster, who represented himself to be "a mechanical and mining engineer and expert on ores and steel and iron properties and their products." . . . Mr. Lancaster made two affidavits in the suit, — the first, a preliminary affidavit, on July 3, 1902, and the second, in more detail, on July 14.

In his first affidavit, Mr. Lancaster stated that he was "familiar with and had made a study of all the various properties and plants" of the Steel Corporation, that the plants and properties could be duplicated for about $300,000,000, and that the total value of all the properties, including good will and organization, was not worth $500,000,000.

Two weeks later, Mr. Lancaster, in his second affidavit, went into the subject of valuation in more detail, and presented the statement upon which this portion of the complainants' case was to depend. He stated, first, that the plants of the Carnegie company, representing 44 per cent of the productive capacity of the Steel Corporation, had been valued on March 12, 1900, by the partners of the Carnegie Steel Company at $75,600,000. This valuation was stated in the answer of the company to Mr. Frick's bill of complaint to be "a full, fair, and accurate valuation of these assets," and also that "the experience and judgment of business men justify us in saying (as we do) that such a method of valuation in large manufacturing companies, and especially of iron and steel in our country, as a rule, is more liberal to the seller than to the buyer; for experience has shown that partnership assets on a just appraisement seldom reach

[1] This was the act of March 28, 1902, under which provisions the plan of exchanging bonds for preferred stock was authorized.

the value at which they stand on the books of the concern." Mr. Lancaster, accepting this statement as accurate, estimated the total value of the Steel Corporation's properties, upon the basis of the 1900 valuation of the Carnegie properties, and including $27,000,000 of Frick Coke Company assets subsequently added, at $200,000,000.

He also presented a table showing the conversion value of the securities of the constituent companies in the securities of the United States Steel Corporation, as follows:

	Common Stock	Preferred Stock	Bonds
Constituent companies	$300,000,000	$247,000,000	$219,000,000
United States Steel Corporation	508,000,000	510,000,000	362,000,000
Increase	$208,000,000	$263,000,000	$143,000,000
Percentage of increase	69	106	65

The inference drawn from this comparison of capitalizations was that, unless the capital of the constituent companies was far below the value of their assets, the capitalization of the United States Steel Corporation greatly exceeded the value which supported its securities. Mr. Lancaster concluded his affidavit by expressing the opinion that the 1902 earnings of the United States Steel Corporation represented the results of an exceptionally prosperous condition of the market, and that many new plants were then building to compete with the corporation in all its departments.

The arguments of complainants' counsel in support of these affidavits were mainly taken up with showing that the iron and steel trade was subject to sudden and extreme reverses and to long periods of depression, and that these contingencies had not been allowed for in the capitalization of the Steel Corporation. They contended: (1) that the value of a group of assets was based on the selling price of those assets, which in turn depended solely upon their earning power, and that, while the Steel Corporation was then earning interest and dividends on all classes of its securities, there was no assurance that these

earnings would be sufficiently permanent to warrant the belief that the selling value of the company's assets could properly be based upon a capitalization of their amount; (2) that the 1902 price of steel was an abnormal price, dependent on temporary conditions, and resulting in earnings which should be disregarded in making an estimate of the ability of the corporation to pay the large increase in interest charges which would result from the success of the conversion plan; (3) they asserted that the directors of the Steel Corporation were about to carry through a plan which was not merely unnecessary and expensive, but dangerous as well, — a plan which would increase its mortgage debt beyond what experience showed would be the minimum value of its assets, a plan whose success spelled bankruptcy, should the history of the steel trade be repeated. The argument of the complainants, in brief, was based entirely on considerations of business probability, and on the results of business experience. Affirming that the requirements of the New Jersey corporation law were designed for the protection of the investor, they asked the court to interpret the meaning of the statute in the light of business probability, and to refuse its sanction to a measure which conservative judgment would disapprove.[1]

This, however, as shown by its refusal to throw out the conversion plan because of its alleged expensiveness, the court was not prepared to do. So long as the requirements of the law were complied with, which in this case meant a certification by the officers of the corporation that its assets, after deducting all indebtedness, were equal in value to the amount of its preferred stock, and in the absence of fraud, the court had no right to interfere.

This certification was furnished in a series of affidavits remarkable because of their prodigal frankness and the varied standards of valuation which they set up. The subject-matter of these affidavits, so far as they relate to the question of assets, may be

[1] Argument of Edward B. Whitney (p. 41): "I submit that the sole object of the Legislature in establishing this restriction as to the amount of assets was to make the recapitalization entirely safe for at least the preferred stock, . . . to secure that in case of insolvency a foreclosure of the new bonds would result in the realization of the full value of the preferred stock if the latter were properly protected."

divided as follows: (1) valuations of property; and (2) estimates of future earnings. The leading affidavit for the defendants was made by Mr. Schwab, who swore to the statement that the total value of the corporation's assets, without making any allowance for good will and established business, patents, trade-marks, and processes, or for $150,000,000 of orders on hand, exceeded the total amount of its capitalization. This statement was not made in general terms, but was supported by a list of assets, giving the value assigned to each and the basis of valuation employed. For purposes of convenience, the material of this affidavit has been arranged in the following table:

Assets	Valuation	Principles governing Valuation
1. Iron and ore properties.	$700,000,000	1. Properties cannot be duplicated at any price. 2. Yield direct profit of $30,000,000 on present price of ore. 3. The Steel Corporation would be compelled to pay $700,000,000 in order to obtain these deposits.
2. Plants, mills, fixtures, machinery, equipment, tools, and real estate.	$300,000,000	1. Impossibility of duplicating these mills for a less amount. 2. The mills are necessary to make the profits of the corporation, stated to be at the rate of $140,000,000 per year.
3. Coal and coke fields (87,589 acres).	$100,000,000	1. Net profits to the corporation, based on the present prices of coal and coke, over $12,000,000.
4. Transportation properties.	$80,000,000 after deducting $40,340,000 of bonded debt.	1. Cost of duplication. 2. Profits of mills increased $10,000,000, because of possession of transportation facilities.
5. Blast furnaces.	$48,000,000	1. Cost of duplication.
6. Natural gas fields.	$20,000,000	1. Profit of $2,000,000.
7. Limestone properties.	$4,000,000	1. Cost of duplication. 2. Profit of $500,000.
8. Cash and cash assets.	$214,278,000	1. Cash assets valued at cost.

Mr. Schwab employs two leading principles in valuing these assets, — (1) cost of duplication and (2) profits derived from their possession. Of his estimate of $140,000,000 as the earnings of the corporation, $54,500,000 is directly accounted for by the savings on ore, coal and coke, transportation, limestone, and natural gas. The direct profits of the mills easily make up the remainder.

Mr. Schwab's affidavit was supplemented by the affidavits of other officials. Mr. Elbert H. Gary, chairman of the Finance Committee, testified that the "intrinsic value" of the properties, as set forth by Mr. Schwab, were true and conservative. Mr. James Gayley, first vice-president, and in general charge of the mining and transportation of raw material, stated in his affidavit that the ore properties of the corporation were not only the most extensive known, but were of such high grade and quality as to make them specially suited to the production of the best quality of iron and steel; and: "that investigations have demonstrated that the deposits of this region are practically circumscribed as to quality, and that, if any new deposits are to be found, it will undoubtedly be at points which are much further removed from sites suited to the economical manufacture and distribution of product," and, further, "that they could not be duplicated or reproduced at any price."

President Lynch, of the Frick Coke Company, supported Mr. Schwab's statement by the assertion that the 315,000,000 tons of coking coal still contained in the Connellsville basin were worth, on a profit of 50 cents per ton, — 75 cents below the profit then being made, — $157,500,000. President James H. Reed of the Pittsburg, Bessemer & Lake Erie Railroad Company, in perhaps the most carefully worded affidavit of the series, affirmed that the cost of the transportation properties of the corporation, after deducting the amount of their bonded debt, was approximately $50,000,000, and that their cost of duplication would be far in excess of this amount, since in many cases it would be impossible to duplicate these facilities. The final affidavit as to the value of the property was made by William J. Filbert, comptroller of the Steel Corporation, who stated that on the basis of the highest prices reached for the two stocks,

the total market value of all the corporation's securities was $1,149,014,932.

The defendants were also at considerable pains to controvert the statements, sworn to in the Carnegie-Frick litigation of 1900, that $75,600,000 represented a "full, fair, and accurate valuation of the Carnegie Steel Company's assets." James J. Campbell, auditor and assistant secretary of the Carnegie company, in his affidavit demolished the truth of the statement made by the defendants in *Frick* v. *The Carnegie Steel Company.* He showed that all the properties of the Carnegie Steel Company had been carried on the books for many years at the original costs, and that no allowance had ever been made for the money expended on them for improvements, which in some instances far exceed the original outlay. The question at issue in the Frick-Carnegie litigation, said Mr. Campbell, did not concern the actual value of the Carnegie company's property, but merely involved the basis of settling for the interests of deceased or withdrawing partners. Mr. Schwab also took the same ground in his affidavit: "It was claimed in such litigation, and such was the fact, that the book value did not represent the actual value of the properties. Under the terms of the agreement to which Mr. Frick was a party, it was provided that the book value should determine the interests of the several associates, and the controversy between Mr. Frick, on the one hand, and Mr. Carnegie and his associates, on the other, was as to whether this nominal book value should control, or the actual value, which Mr. Frick alleged to be in excess of $250,000,000."

The defendants did not stop with estimates of present valuation. They accepted the standard of business probability which the complainants claimed should be applied to determine the value of the Steel Corporation's assets, and asserted that, in their judgment, the earnings of the Steel Corporation would never fall so low as to endanger the interest on the second mortgage bonds. As a matter of record, these predictions should be preserved.

Mr. Schwab stated that, if the conversion plan were carried through, the fixed charges of the corporation — he makes no allowance for depreciation — would be $31,737,850. The earn-

ings of the corporation were then more than four and one-half times this amount, leaving a margin of 75 per cent above the danger of bankruptcy. "The most careful investigation," said Mr. Schwab, "was made at the time the board of directors voted to recommend the issue of $250,000,000 of second mortgage bonds, to determine whether, under any reasonable possible conditions, the earnings of the Steel Corporation would be reduced below the total fixed charges of $31,737,850. The unanimous opinion of the officers and directors who had a lifetime of experience in the business was that, under no conditions of the iron and steel trade or of business depression, was there any reasonable likelihood that the earning capacity of these vast properties would be reduced to any such extent." This part of Mr. Schwab's affidavit was repeated in almost identical terms by Mr. Gary, who stated that the board of directors was unanimously of this opinion. It is unfortunate that these vigorous statements do not start from an assumption of at least $60,000,000 of fixed charges, for, on Mr. Schwab's basis of valuation, a $30,000,000 charge for depreciation would be none too large.

Under the weight of this mountain of testimony, the arguments of the complainants, which they admitted were founded on "*ex-parte* and argumentative affidavits," were crushed to the ground. They were forced to admit that their part of the case was in a condition far from satisfactory, and, in fact, were unable to bring any rebuttal evidence or argument worthy of comment, contenting themselves with repeating their original contentions.[1]

Furthermore, the appearance of Mr. Lancaster in the case gave the defendants an opportunity to impeach the good faith of the suit, which they did not fail to improve. As an illustration of the motives which animate the movers in these so-called "strike suits," of which it was charged that this was an example,[2] a portion of

[1] Extract from Section VIII of Brief for Complainants on Appeal: "The complainants' papers at the commencement of this litigation were necessarily prepared hastily, and it is obvious that great labor and a long time would be required, especially for parties not having access to the books and papers of the corporation, to make an inventory of the property, even approximately accurate. . . . We frankly concede that the record on the question of value is not in a satisfactory condition from the complainants' point of view."

[2] See page 176 *infra*.

the affidavit of Joseph E. Corrigan, an attorney in the office of Guthrie, Cravath & Henderson, may be advantageously presented. Mr. Corrigan stated that on August 15 Mr. Lancaster, on his own initiative, made to him and Mr. Guthrie substantially the following statement:

"That on the third day of July, 1902, a young man named Preskauer handed them the business card of the law firm of James, Schell & Elkus, and told him that Mr. Elkus wanted to see him at his (Elkus') office. That he at once proceeded to said office, and there for the first time met Mr. Elkus whom he had never known before. That he was introduced by Mr. Elkus to David Lamar, that said Lamar thereupon talked to him in the presence of said Elkus about the United States Steel Corporation's properties and their values, and after some conversation said that he desired an affidavit as to the values; that said Lancaster did not know and was not told that the affidavit was to be used in litigation, and did not observe any title of a suit, to what at the time he swore to. That he protested that it was impossible for him in so short a time to make an affidavit; but that said Lamar said they would be satisfied with his present impressions, and what he knew generally about the steel business; and that they would give him $100 for the affidavit. Said Lancaster further stated that he needed the money, and that, as this was an easy way to make $100, he was willing to swear to the affidavit, although he did not know what it was to be used for, and supposed it was simply for said Lamar's information, or for some purpose said Lamar had in mind, and that he gathered from what Lamar said to him that it was to be a guide for investing in stocks. Said Lancaster further stated to Mr. Guthrie and myself that, a few days afterwards, he for the first time ascertained that his affidavit had been used in a suit against the United States Steel Corporation. That he went at once and protested to Mr. Lamar . . . that he had been deceived. Said Lamar thereupon agreed to pay him $250 a week and $10,000 when they succeeded in making a settlement, which he (Lamar) assured Lancaster would not be later than November 1. That he made a second affidavit in the suit, for which he was paid $400. That he then had a row with Lamar over the subject of

his compensation, that he threatened to expose them all, and that finally Lamar agreed to pay him $500, making $1000 in all, provided said Lancaster would execute a general release and sign a letter to the effect that he would not disclose to any one what had occurred in Mr. Elkus' office — that he understood from what Mr. Lamar and others said in Mr. Elkus' office that they expected to make big money out of the suit, and that a number of the suits were in preparation and would be brought one after another until a settlement was forced."[1]

The weight of the argument as to the value of the Steel Corporation's assets was plainly with the defendants. Vice-Chancellor Emery supported their contention at every point. He stated in his opinion that the certificate of value required by the law had been filed by the proper officers, and that "upon the affidavits filed there can be no question whatever as to their honesty and good faith in making this certificate as to value." This certificate, it is true, was not conclusive evidence, but might be shown to be false. The proof of its falsity, however, in this case, had not been furnished. The affidavits filed by the defendant company, said the Vice-Chancellor, on this question of the value of the assets, are "full, complete, and detailed, and are made by persons entirely familiar with the property, or portions of the property, as to whose value they affirm. The affidavits as to value filed by complainant are, on the other hand, general, vague, and made without special knowledge or examination, and the credibility of the principal affiant on the part of the complainant is seriously impaired by his own admissions in his latest affidavit. Upon these affidavits as to value, I would not be justified in enjoining the issue of the bonds, pending the final hearing." The Court of Appeals, while passing upon the arguments of the complainant, apparently did not consider the discussion of the value of assets of sufficient importance to even refer to it.

The United States Steel Corporation, in the Hodge suit, won a complete victory. Its opponents were not merely routed, but

[1] Lancaster, in a supplementary affidavit, denied the correctness of some of Mr. Corrigan's statements, but admits their general correctness, and places himself in a generally unfavorable light.

the honesty of their motives was seriously impugned. The legality, and, so far as the court went in this direction, the wisdom of the plan for converting bonds into stock, were upheld. The vindication of the defendants could not have been more complete.

There is, however, another side to the question. Apart from the provisions of the New Jersey corporation act which the directors were careful to obey, the facts brought out by the Berger and Hodge suits constitute a serious indictment of the wisdom of the bond conversion plan. Surely, at this late day, few will be found to indorse a plan to change a dividend requirement on $200,000,000 of stock into an interest requirement on $200,000,000 of bonds, for no better reason than to save the interest and sinking fund charges on an additional $50,000,000 of bonds. The mere statement of the plan, which runs directly against every recognized canon of corporation finance, is sufficient to secure its condemnation. The proposal ignored the mortgage lien of the bonds which were to be substituted for stock, and the fact that with the issue of the new bonds the borrowing capacity of the corporation would be exhausted, for the sake of saving $4,000,000 in dividend payments, 2 per cent of the net profits of the company in 1902.

We have become familiar with plans for the conversion of bonds into stock where the purpose is to reduce fixed charges. Projects for purchasing stock with bonds secured by the stock — for example, the purchase of Burlington, Jersey Central, and Louisville & Nashville — are not uncommon. In such cases, the purchasing company can apply the dividends on the stock to the payment of interest on the new bonds; and the lien, aside from a guarantee which can be enforced only with great difficulty, is on the stock which the bonds were issued to purchase. Such projects have to commend them either the reduction of fixed charges, or the gaining control of companies where control means a large increase in the earnings of the parent corporation. But to propose a conversion scheme for no better reason than to reduce dividends in favor of interest, is a proposition which has little to commend it.

Then, too, can the syndicate agreement, when drawn from under the healing wings of the stockholders' approval, stand the test of critical examination? The theory advanced by defendants' counsel, that the amount of the syndicate's compensation should be determined, not by the benefit to the corporation, but by the risk of the syndicate, would seem to be untenable. Underwriting syndicates are usually supposed to guarantee cash. Their commission is based upon the amount of cash for which they are liable. The maximum commission in the case under consideration was 44 per cent of the cash guarantee, — an amount out of proportion to the benefit received. The argument that it was necessary to sequester a large amount of preferred stock in advance of the announcement of the conversion plan, because of the practical certainty that the announcement would raise the price of the preferred stock above par and make conversion undesirable, is singularly weak. In what manner the placing of $12,500,000 of interest charges ahead of the preferred stock dividends, would advance the value of the latter security, can better be imagined than described. The course of the preferred stock since the conversion plan was announced offers an interesting commentary upon the prescience of the Finance Committee.

Space does not permit an extended examination of the methods employed in valuing the assets of the Steel Corporation. At the time these affidavits were made, there can be no question that, as worded, they deserved the high praise awarded them by the Vice-Chancellor, of being full, complete, and detailed, and of being made in honesty and good faith. In July, 1902, the corporation was earning at the rate of $140,000,000 per year; and the "present worth" of its assets, which is the plain meaning of the law, was in excess of $1,400,000,000. If the argument of the complainants was to stand, the law should have read something as follows: "that no corporation shall be permitted to retire its preferred stock by the issue of bonds whose earnings, in the judgment of some competent tribunal, shall not at all times be adequate to pay dividends on the preferred stock." In such an event, however, the question would never have come before the court in the course of litigation.

It would have been definitely settled beforehand. As the law stands, and looking only to present value, the adequacy of Steel Corporation's assets in July, 1902, to conform to the requirements is evident.

But what shall be said of the wisdom of the policy which accepts such a valuation as a basis for incurring $10,000,000 additional of fixed charges without corresponding increase of assets? The fixed charges of the Steel Corporation, assuming that the conversion scheme had been a complete success, and making adequate allowance for depreciation, would have been at least $70,000,000 per year. As they now stand, with only $150,000,000 of preferred stock exchanged, they are not far from $65,000,000.[1] Here is a necessary reduction in earnings before the limit of fixed charges is reached, not of 75 per cent, as stated in the directors' affidavits, but of 50 per cent. There will be few persons found, who are in any way conversant with the history of the steel trade, to affirm that the earnings of any steel corporation could not be reduced one-half by a very moderate decline in prices. The Steel Corporation averaged a profit of $16 per ton during 1902. It may fairly be questioned whether the conditions of competition and demand warrant the proposition that a profit of $8 per ton can be secured when the trade is at its lowest ebb.

As above remarked, however, while the directors were ready to swear to the belief that the profits of the Steel Corporation would never be reduced as low as $31,000,000, they included no allowance for depreciation in their estimate of fixed charges. Their judgment would not, therefore, be impeached, should the earnings of the Steel Corporation fall below its fixed charges. If the rule be accepted, however, — that, in issuing bonds, a corporation should always maintain a wide margin between minimum net earnings and fixed charges, — it is impossible to approve a plan to add $12,500,000 to the interest charges of

[1] This statement is not based upon official announcements, but upon common report at the time the life of the syndicate was extended. If the gap between preferred stock and bonds is not closed, there is every reason to expect that the operations of the syndicate in purchasing preferred stock for retirement will insure the final success of the plan of commission.

the United States Steel Corporation. The fixed charges of the company were too high before for entire safety. The issue of $250,000,000 of bonds, or even $150,000,000, can be described by no other word than unwise.

The Hodge and Berger suits may have been inspired by improper motives, but they have served to call attention to certain glaring defects in American corporation law. The time has gone by when the determination of great questions of corporate policy, involving the welfare of the community as well as the interests of stockholders, can be safely left to their own judgment. The average stockholder in corporations such as the Steel Corporation is incapable of forming a judgment on questions such as those under discussion. He is one of a flock of sheep who follow first one false shepherd and then another, until, inverting the parable, for every sheep that is safely folded, ninety-and-nine are hopelessly led astray. He invests because he has confidence in some individual. Unfortunately, his confidence is frequently misplaced. The laws of those states, such as New Jersey, in which most large companies are incorporated, give the stockholders abundant protection against directors and officers who attempt, by concealment and fraud, to violate their trust. These laws, however, give no protection to the stockholder against his own ignorance and credulity. If the stockholder was the only one to suffer the consequences of his own simplicity, there might be no reason for advocating a plan of federal control which would compel directors to follow a conservative policy in the distribution of earnings and the readjustment of capital. But where the history of each day is furnishing new evidence that the prosperity of the community is jeopardized by reckless financiering, it is plain that the people should, for their own protection, take out of the hands of stockholders the control of matters with which they are incompetent to deal, and by the enactment of laws similar to those which regulate the conduct of national banks, compel directors to keep at all times within the limits of conservatism.

If the tremendous decline in the securities of the largest industrial corporation in the world — a decline which is almost without parallel, and which has inflicted heavy losses upon tens

of thousands of stockholders — shall furnish the object-lesson necessary to bring the American people to their senses upon this question of the necessity of rigid federal control of large corporations, the United States Steel Corporation will not have lived in vain.

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THE STEEL CORPORATION'S BOND CONVERSION: A CORRECTION[1]

In the preceding article Professor Meade gives prominence to the recent suit of Mr. Hodge against the Steel Corporation, referring to it as if it might have been a "strike suit." That the defendants in this suit could obtain a withdrawal without pecuniary outlay was well known to them. Mr. Hodge's offer of withdrawal, made through me in writing at an early stage of the litigation, asked simply a resubmission of the scheme to the stockholders with full information as to its main features, or else its modification by taking from the Morgan syndicate all advantage over the other preferred stockholders, giving it no longer option to subscribe for the bonds, no greater time to pay subscriptions, and no commission except upon the amount which the syndicate should absolutely bind itself to underwrite.

The point upon which the Vice-Chancellor decided the case in Mr. Hodge's favor, if sustained, would have forced a resubmission to the stockholders. It would probably then have been voted down. The notice upon which their proxies had been obtained had been so drawn as to give the impression that the whole bond issue had been underwritten; and the syndicate's extraordinary option was not apparent. The stockholders were indeed informed that by calling at the Morgan office they could secure complete copies of the proposed contract; but, as Professor Meade truly says, nobody called. Each assumed that he had enough information, and did not need to examine legal documents. The most interesting question to the public in the

[1] From the *Quarterly Journal of Economics*, Vol. XVIII, 1904, p. 303.

Hodge suit was whether this notice sufficiently discharged the duties of the directors. The New Jersey court held that it did. Other courts have set up a much higher standard, and required of interested directors the fullest disclosure. The standard set by the state which has fathered so large a proportion of the modern "trusts" has had no small influence upon public confidence in their securities.

Time has already vindicated Mr. Hodge. Public sentiment recognizes this, and has forced the surrender of the syndicate option. Mr. Schwab's valuations have been condemned by the market, and by the abandonment of dividends, to the loss of so many common stockholders. The principle of his valuation, that in bonding a company it should be capitalized on the basis of the profits of a year of prosperity, instead of upon the availability of its assets in a period of depression, was never indorsed by conservative men, although it passed muster with the New Jersey courts.

The fact that Mr. Hodge was publicly joined as complainant by no other stockholder of record was not due to lack of sympathy, — of that he received a plenty, — but to two conditions which are among those that most contribute to the success of the modern "trust" financier. Persons with large interests at stake cannot afford to join openly, because they are afraid that the dominant powers in Wall street may take revenge by attacking their financial credit and excluding them from profitable enterprises. Small stockholders have not sufficient interest pecuniarily to justify the annoyance and notoriety and the newspaper abuse to which they would be subjected. Even necessary expert testimony is difficult and expensive to obtain, through fear of boycott; and the swiftness with which the directors' plans are carried through after their announcement leaves stockholders but little time for consultation and none for deliberate action. It is only when the plans fail for other causes, as in the shipbuilding case, that the minority have time for investigation or combined action.

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THE BOND-CONVERSION PLAN OF 1902-3.[1]

Extent of Conversion Operations

At the time the conversion plan was first announced, in April, 1902, the syndicate members deposited with the syndicate managers $80,000,000 preferred stock, and it appears that this stock was allowed to remain in the hands of the syndicate managers during the time the plan was delayed by litigation. There were deposited by stockholders outside of the syndicate, either at the time the plan was originally announced or under the offer as renewed a year later, $45,200,000 of preferred stock.[2] There were no cash subscriptions to new bonds on the part of individual stockholders outside of the syndicate (except for the trifling amount of $12,200), since the bonds at the outset sold (on a "when-issued" basis) slightly under par and were selling by March, 1903, when the plan was formally put in operation, at only 88. The preferred stock was selling in April, 1902, when the plan was first announced, at 94; by the time the offer was renewed the price had dropped to about 85.

Under the offer as renewed, the right to exchange preferred stock for bonds, so far as shareholders outside of the syndicate were concerned, was to cease on May 16, 1903. The underwriting syndicate, however, could make such exchange until July 1, 1904; in other words, for a period of 13½ months after this privilege was terminated with respect to the stockholders outside the syndicate. It is true that the individual stockholders had been given for a limited period a preferential opportunity to exchange their preferred stock for bonds. That is to say, had every holder of preferred stock outside of the syndicate elected to exchange 40 per cent of his preferred stock for bonds, then the syndicate would have been able to exchange only a part (about 40 per cent) of the $80,000,000 which it had deposited with J. P. Morgan & Co. As just shown, however, only about $45,200,000 of preferred stock was deposited by the shareholders outside the syndicate up to May 16, 1903, when the privi-

[1] From U. S. Commissioner of Corporations, Report on the Steel Industry, I, July 1, 1911, p. 348-358.

[2] Annual report of the Steel Corporation for 1903.

lege was terminated so far as these stockholders were concerned. On the other hand, the syndicate, under its arrangement, was to be allowed to continue such exchanges up to July 1, 1904.

The exclusive extension of this privilege to the underwriting syndicate for this period resulted in intense dissatisfaction. This was greatly aggravated because the margin between the price of the bonds and the price of the preferred stock continued to widen, so that the syndicate was able to make a large profit by buying the preferred stock in the market and immediately turning it into bonds worth a higher price. (As shown elsewhere, the profit on this operation may have been more than offset by a loss on the syndicate's cash subscription to $20,000,000 bonds.) In October, 1903, the margin between the price of the bonds and the price of the preferred stock was about 12 points. In November it widened out to 15 points, the preferred stock selling below 50, whereas the lowest price for the bonds was 65. This meant that the syndicate, which had the exclusive right to continue the conversion, could, by buying preferred stock in the open market and immediately exchanging it for the new bonds, make a profit of $12 to $15 on every share thus purchased and exchanged. The total amount of the stock purchased by the syndicate appears to have been about 248,000 shares.

The fact that the privilege of such exchange was confined to the underwriting syndicate, as well as other features of the plan, aroused widespread disapproval. As a result, on November 19, 1903, the arrangement was abruptly terminated.

Results of Conversion Plan

Results to the Corporation. — The conversion plan, it will be recalled, purported to provide for the exchange of $200,000,000 of 7 per cent preferred stock into a like amount of 5 per cent bonds, thereby substituting an interest charge of $10,000,000 for dividend requirements of $14,000,000, and also for the sale of $50,000,000 of bonds to provide cash, which was apparently much needed, thereby increasing the interest charges by $2,500,000. One result of this plan, therefore, had it been

carried out in its entirety, would have been the substitution of $12,500,000 of interest for $14,000,000 of dividends, or a net saving to the Corporation of $1,500,000. On the conversion alone the saving would have been $4,000,000. As already seen, however, this object was by no means realized. The total amount of bonds issued under this conversion plan was stated by Chairman Gary, at the time the syndicate agreement was terminated, as follows:

$146,388,500	bonds have already been issued in exchange for stock received and canceled.
3,611,500	remain to be issued in exchange for preferred stock to be converted by the syndicate.
2,902,000	bonds sold at par for cash and paid for in full October 1 and already issued.
17,098,000	bonds sold at par for cash upon which 25 per cent was paid to the Corporation October 1 and which will be issued whenever the remaining 75 per cent shall be called for and paid.
170,000,000	total issue outstanding.

The arrangement was further described in the second annual report of the Corporation as follows:

Up to December 31, 1903, there had been issued and were outstanding United States Steel Corporation 10–60 year 5 per cent sinking fund gold bonds, dated April 1, 1903, for the aggregate principal sum of $152,902,500. These bonds were issued in payment for 1,500,000 shares of preferred stock at par, as well as in consideration of $7,177,100 cash received from J. P. Morgan & Co., for a syndicate, being part of $20,000,000 cash receivable under the contract of April 1, 1902, approved by the stockholders in special meeting May 19, 1902, and thereafter sustained by the courts. Since January 1, 1904, and up to the date of the writing of this report, there have been received from J. P. Morgan & Co. $3,822,900 additional on account of the aggregate of $20,000,000 cash receivable as above, and there have been issued additional bonds of the par value of $5,097,500, making at this date (March 1, 1904) a total issue of bonds for the aggregate principal sum of $158,000,000. Thus the Corporation has received from J. P. Morgan & Co. for the syndicate $11,000,000 in cash and has delivered $8,000,000 in bonds, leaving $9,000,000 cash to be received and $12,000,000 bonds to be delivered.

The Corporation has the right at its option at any time to call for

the remaining $9,000,000 cash, but in order to avoid the unnecessary burden of interest upon bonds issued for money not immediately needed, arrangements have been made with J. P. Morgan & Co. whereby, until otherwise provided, the Corporation will not be required to call the remaining $9,000,000 cash or to deliver bonds therefor except when and as the cash shall be needed by the Corporation. Interest on these bonds begins to run only as and when the Corporation receives cash for them. Under Article Third of the contract, Messrs. J. P. Morgan & Co., representing the syndicate, have received, or will receive, as compensation 4 per cent upon the par of $170,000,000 bonds, for which there have been sold to and received by the Corporation 1,500,000 shares of preferred stock at par, besides the $20,000,000 in cash received or receivable as above stated.

It will be seen, therefore, that the plan fell far short of accomplishing what it was designed to accomplish. Instead of providing $50,000,000 new cash (or, after deducting the syndicate's commission of 4 per cent, a net amount of $40,000,000) the total new cash raised was only $13,200,000, this amount being arrived at by deducting from the $20,000,000 cash subscribed by the syndicate the 4 per cent commission on the total of $170,000,000 of new bonds issued, or $6,800,000. Moreover, only a portion of this cash had been paid in to the Corporation at the end of December, 1903, whereas, according to the circular announcing the conversion plan in April, 1902, $50,000,000 of cash was desired in the immediate future. The annual dividend requirements of the Corporation had been reduced by $10,500,000 through the exchange of the $150,000,000 of 7 per cent preferred stock for the 5 per cent bonds, but interest charges had been increased $8,500,000 by reason of the issuance of a corresponding amount of 5 per cent bonds plus $20,000,000 additional bonds sold for cash. There was, therefore, a net reduction in the combined charges of $2,000,000 per annum This reduction, however, had been accomplished only by substituting a bonded debt for a stock liability, and at an initial cash expenditure of $6,800,000 for commissions.

Results to the Syndicate. — The results of the bond-conversion plan to the underwriting syndicate can only be estimated, since it is not known what the stock deposited by syndicate members

cost them, or what profit was made on the purchase of preferred stock in the open market by the syndicate for exchange into bonds.

It will be recalled that the syndicate originally deposited $80,000,000 of preferred stock and the outside stockholders $45,200,000, leaving $24,800,000 to be purchased in the open market by the syndicate (the total amount of preferred stock exchanged being $150,000,000).

The preferred stock, at the time it was originally deposited by the syndicate members, was worth, as already stated, about 94. The 5 per cent bonds, at the time the syndicate was finally wound up in May, 1904, were quoted at about 73. On this basis alone (which is not wholly conclusive), there was a loss of 21 points on each share of preferred stock exchanged by the syndicate, or $16,800,000 in all. Against this, however, must be placed the syndicate's commission of $6,800,000, and the profits which it made on the purchase of preferred stock in the open market for exchange into bonds; deductions would then have to be made for certain expenses of the syndicate. The amount of the profit made on such purchases of preferred stock in the open market is not definitely known. Just before the conversion arrangement was terminated, in the latter part of November, 1903, there was a possible profit of nearly 15 points on such conversion operations. As shown later, very heavy purchases of the preferred stock were made in the open market at just about this time, and it is reasonable to assume that a considerable part of such purchases were for the account of the syndicate, because of the large profit possible on such operations. An allowance of $15 per share as the average profit on such open-market conversion operations would, however, probably be too high. Assuming that the profit may have averaged as much as $10 per share for the preferred stock exchanged, the syndicate's profit on this part of the transaction would have been, roughly, $2,500,000, in addition to which there would have been some interest receipts; but, on the other hand, there would have to be deducted the expenses of the syndicate. Assuming that the net profit on the preferred stock purchased for exchange into bonds was only $2,000,000, the indicated loss of $16,800,000

above referred to would have been reduced, after also taking account of the $6,800,000 commission, to $8,000,000. It may be noted that some estimates of the syndicate's loss published in financial journals about this time ranged in the neighborhood of this figure.

It is, of course, somewhat arbitrary to calculate the results to the syndicate on the basis of the value of the bonds on the day the syndicate agreement was terminated. Some of the bonds had been delivered to syndicate members prior to that date, while the value of those received at that time might perhaps be better expressed by taking the average market price over a considerable period of time. Thus the average price of these bonds during the remainder of the calendar year 1904 was approximately 81, or 8 points above the price used in the foregoing calculation. If the bonds had been disposed of at such an average figure, the indicated loss would of course, be correspondingly reduced.

Any calculations of the results to the syndicate, however, are necessarily somewhat inconclusive. The conversion operations were accompanied by pronounced depression in the steel industry and there can be little doubt that the preferred stock would have declined heavily even had the conversion plan never been undertaken. Viewed from this standpoint, it might be argued that the syndicate members (and individual stockholders as well), in proportion as they exchanged preferred stock for a bond worth from 10 to 15 points more, reduced a loss which they might otherwise have suffered. On the other hand, in recent years the preferred stock of the Steel Corporation has sold well above these bonds (both issues, moreover, having sold for a long time well above par), so that viewed from this point it might be argued that the stockholders and syndicate members who exchanged their preferred stock had lost a possible profit in this operation. Against any sacrifice of future profit which might have been made by retaining the 7 per cent preferred stock, however, those who exchanged that issue at all times enjoyed the advantages afforded by a security which preceded that issue, while, moreover, the bonds for a considerable time sold at higher prices than the preferred stock.

General Criticism of the Conversion Plan

While the courts of final resort decided every suit brought against the conversion plan in favor of the United States Steel Corporation, their decisions really had almost nothing to do with the merits of the plan itself. The courts passed almost exclusively on the legal rights of the Corporation. On the question of the propriety of the plan the court simply held that, in the absence of fraud, they could not go back of the action of the directors of the Corporation. They held that there was no evidence of fraud. This, however, is aside from the question of the advisability or wisdom of the plan.

The wisdom of substituting a bond issue for a portion of the preferred stock may be left to individual opinion. The question whether the company should have postponed the payment of dividends on the common stock and thus have avoided issuing bonds for cash may likewise be passed over at this late day, and particularly since these are matters which concern the stockholders rather than the general public. Some features of the plan, however, are of general interest both as bearing upon the organization and financing of corporations, and also because they had a direct bearing through the stock market on the security market in general, and thus tended directly to affect the general public. Particular mention may be made of the arrangement with the underwriting syndicate and its compensation. It will be recalled that whereas the holders of the preferred stock outside the syndicate were permitted to deposit preferred stock in exchange for bonds only during the period from March 16 to May 16, 1903, the syndicate was, under the terms of the contract, as renewed, permitted to make such exchange up to July 1, 1904. After the offer had been terminated with respect to the shareholders outside the syndicate, in view of the fact that such shareholders took advantage of the offer only to a limited extent, the decline in the market price of the preferred stock worked to the advantage of the syndicate, since it could buy that stock and convert it into bonds at a higher price. While the bonds themselves declined greatly in value the preferred stock fell so much faster that there was a large profit for the

syndicate (with respect to this part of the arrangement) in thus purchasing preferred stock and exchanging it into bonds. As already shown, when the plan was first announced, in April, 1902, the new bonds were quoted at only a fraction under par, the preferred stock at 94. By the time the plan was actually put in operation, in March, 1903, the preferred stock had dropped to about 86. The bonds, however, had fallen to about 87, so that there was only a small margin between them. The relationship of the two prices was substantially maintained up to May 16, 1903, when the subscription privilege of preferred stockholders outside the syndicate was terminated, both the stock and the bonds being quoted on that date at about 83. By July 1, however, the stock had fallen to 81, the bonds remaining unchanged at about 83, thus showing a difference of about 2 points. By the first of October this margin had increased to about 10 points, and by the end of the month to over 12 points, while by the middle of November, or just before the contract with the syndicate was terminated, it had widened out to about 15 points. During the entire interval from May 16, 1903, to November 19, 1903, on which date the arrangement was terminated, the syndicate had the exclusive right of conversion. Obviously there was a heavy profit in thus purchasing preferred stock at from 10 to 15 points below the price of the bonds and making the conversion. It has already been shown that the syndicate apparently purchased something like 248,000 shares of preferred stock in addition to the amount originally deposited by it. Apparently the great bulk of this stock was purchased during the interval when the margin between the price of the bonds and the price of the stock was abnormally wide. Very convincing evidence to this effect is furnished by the fact that on October 22, 1903, the United States Steel Corporation, in making application to the New York Stock Exchange to have these bonds listed on the exchange, stated that there had been issued up to that time $133,295,500 of the new bonds, of which amount $130,411,000 had been issued in exchange for preferred stock to be retired (the balance having been sold for cash to the syndicate). As above shown, when the syndicate agreement was terminated by the Corporation, the amount of preferred stock exchanged or

which could be exchanged was $150,000,000. Therefore, the evidence is very strong that during this interval between October 22, 1903, and November 19, 1903, approximately $20,000,000 worth of preferred stock, or 200,000 shares, were purchased in the open market by the syndicate for exchange. During this interval there were very heavy transactions in the preferred stock, the total for the four weeks ended October 19 exceeding 2,000,000 shares, while the margin between the preferred stock and the bonds ranged generally from 12 to 15 points, occasionally being somewhat greater.

As already stated the privilege of the syndicate to make such conversion operations was terminated on November 19, 1903. The following statement was given out by E. H. Gary, chairman of the Corporation:

> At a meeting of the finance committee of the United States Steel Corporation held yesterday it was (by unanimous vote) decided to suggest to Messrs. J. P. Morgan & Co. that the syndicate contract for the conversion of preferred stock into second-mortgage 5 per cent bonds should be canceled and terminated beyond the amount of $150,000,000, which figure has very nearly been reached.
>
> Messrs. J. P. Morgan & Co. immediately acceded to the request of the finance committee and no further exchanges will be made for account of the syndicate beyond the amount stated.

It was reported that this sudden termination of the agreement was prompted by the threat of injunction proceedings against the Corporation. However that may have been, the vigorous condemnation of the plan by the press was involving the Corporation in exceedingly unpleasant notoriety, and there can be little doubt that the abandonment of the arrangement was in response to this disapproval. (See pp. 350–351.)

While the evidence, therefore, indicates that the syndicate purchased a very large quantity of preferred stock during the period when it was selling at a wide margin under the price of the bonds, this in itself does not show that the syndicate was directly responsible for the pronounced depression of the stock Such charges would, of course, be almost impossible of proof. It is, however, worth noting that the suspicion was very widely

entertained in Wall Street at the time that the syndicate was not merely taking advantage of a pronounced decline in the preferred stock, but that it had actively assisted in bringing about this decline. The mere fact that there was a special inducement to indulge in such manipulation and that the syndicate would be the sole beneficiary at the expense of the remaining stockholders is alone a very telling criticism of this feature of the plan.

Complaint was also made that the 4 per cent commission to the syndicate was excessive. Opinions on this question depend chiefly on one's views as to the general merit of the plan of exchanging preferred stock into bonds. If the conclusion be reached that the substitution of $150,000,000 of 5 per cent bonds for a like amount of 7 per cent preferred stock was in itself desirable and advantageous to the Corporation, then the payment of $6,800,000 in the form of a 4 per cent commission on this portion of the bond issue could perhaps be defended. If, however, such substitution of bonds for stock is regarded as inadvisable, then the payment of the 4 per cent commission for effecting such exchange becomes open to objection. It amounted, on this assumption, to the payment by the Corporation of $6,800,000 to the syndicate for raising $20,000,000 of cash; in other words, a commission of 34 per cent. Viewed in this light alone, it is impossible to avoid the conclusion that the commission was grossly excessive.

Without attempting to pass on this feature of the plan, it seems clear that the exclusive privilege allowed the syndicate of converting preferred stock into bonds was undesirable and unjustifiable. Certainly for the time being it seriously hurt the prestige of the Corporation.

Reasons for the Conversion Plan.—There has been a great deal of discussion as to why the directors of the Steel Corporation decided upon this conversion plan. One of the most probable reasons for its adoption is that the financial interests identified with the Corporation found that its enormous capitalization acted as a wet blanket upon the stock market at all times and, furthermore, that it constituted a very serious potential menace in the event of a sudden panic. Although the preferred

stock of the Corporation was paying 7 per cent dividends, it was at that time regarded by conservative investors as distinctly a speculative security. Indeed, during the depression in the iron and steel industry in the winter of 1903–1904, when the dividend on the common stock was first cut in two, and later suspended altogether, there were very grave fears that the Corporation would not be able to maintain dividends on even the preferred stock. This feeling among conservative investors undoubtedly prevented a rapid distribution of the preferred issue by banking interests who were carrying large amounts of this stock. A 5 per cent bond, on the other hand, might appeal more strongly to the investing class, and thus might afford a means for relieving the stock market of the pressure of the enormous capitalization of the Corporation to that extent. That is to say, if a large amount of the preferred stock of the Corporation then "on the market" could be withdrawn, exchanged into bonds, and placed with investors who would be disposed to hold the latter without much regard to temporary fluctuations in market conditions, the financial operations of banking interests in other directions would be facilitated to this extent. A special point in this connection is that some of the large insurance corporations, and other institutions of a similar character, might naturally be more ready to purchase a bond than preferred stock. There seems to be little doubt that this was a primary motive underlying the adoption of the conversion plan.

Another explanation sometimes advanced is that the plan was largely designed to increase the value of the common stock by reducing the prior charges. Some of the leading interests in the Steel Corporation claimed to be large owners of the common stock. It is difficult to believe, however, that this could have been a very important consideration in the minds of the directors, since the substitution of a bonded debt for the preferred stock can hardly be regarded as likely to improve the standing of the common stock with investors generally. It is true that the new bonds contained a provision to the effect that foreclosure proceedings could not be instituted under them until there had been a failure for a consecutive period of two years to pay interest. It is also true that the conversion operations reduced the

charges coming ahead of the common stock. However, the influence of a bond issue is ordinarily more adverse to the common stock than that of an issue of preferred stock, and it hardly seems probable that the possibility of enhancing the value of the common stock was an important factor in bringing about this conversion plan.

Still another explanation offered for this plan was that it was a deliberate scheme to enable the underwriting syndicate to "milk" the Corporation. While the anticipated profit of the syndicate undoubtedly was an important consideration, and while, as already pointed out, such underwriting profits were a very conspicuous feature of the consolidation movement in the steel industry throughout, it hardly seems reasonable to assume that the primary object of the directors of the Corporation in adopting this conversion plan was to secure a large profit for an underwriting syndicate of which only a part of them were members. While open to several serious objections, it seems more probable that the syndicate arrangement was an incident of the plan and not its chief object.

VIII

THE TOBACCO MONOPOLY[1]

HISTORY OF THE TOBACCO COMBINATION

THE Tobacco combination has as its center the American Tobacco Company. This company controls three great subsidiary combinations — the American Snuff Company, the American Cigar Company, and the British-American Tobacco Company. The American Tobacco Company and the other three combinations each control a large number of subsidiary companies. The number of companies in the combination doing business in the United States, Porto Rico, and Cuba is 86, besides a considerable number operating only in foreign countries.

The Tobacco combination dominates the tobacco industry of the United States. With the exception of cigars, its proportion of the country's output of manufactured tobacco products is substantially four fifths, giving it a large degree of monopoly power.

The magnitude of the combination is further shown by its enormous capitalization. The said 86 companies have an aggregate capitalization, including bonds, of $450,395,890. A considerable part of this, however, represents duplication through intercompany ownership of securities. The net amount of the stock and bonds of the companies in the hands of the public (including the directors and all holders except the companies themselves), however, is no less than $316,346,821.

The American Tobacco Company and its Cigarette Monopoly, 1890 to 1895

The history of the combination begins with the organization of the American Tobacco Company in 1890. This was a combination of the five principal manufacturers of cigarettes, and

[1] From Report U. S. Commissioner of Corporations, vol. I, Feb. 25, 1909, pp. 1-41. Footnotes and subheadings are omitted without specific indication. Compare also the Supreme Court decision of 1911 in Chapter XVII, *infra*.

its business at first was confined substantially to cigarette manufacture. The company started with a capital of $10,000,000 of preferred stock and $15,000,000 of common stock — an amount vastly in excess of its tangible assets, which were $5,000,000 (including $1,825,000 in the form of notes of the individual stockholders). James B. Duke was made president, and from that time to this he has been president of the leading companies in the combination and has largely directed its policy.

The American Tobacco Company at its inception secured control of over 90 per cent of the cigarette business of the country. It sought to maintain this dominant position partly by making agreements for the exclusive use of what were considered the best cigarette machines; the most important of these agreements, however, was terminated in 1895. During this period, 1890 to 1895, the average profits of the company were very large, exceeding four million dollars annually.

The Plug-tobacco War, 1894 to 1897

The American Tobacco Company early began to extend its domination to cover other branches of the tobacco industry. In 1891 the authorized capital was increased to $35,000,000. Of this increase $6,000,000 was common and $4,000,000 preferred stock. In this year the company bought two important concerns manufacturing smoking tobacco and snuff, another manufacturing plug chewing tobacco, and a fourth which was the principal manufacturer of cheroots in the United States. During the period from 1894 to 1897 it developed its plug-tobacco business with such a degree of success that ultimately its leading competitors in that branch were forced into combination with itself.

In pursuit of its policy of expansion the American Tobacco Company, particularly after 1894, sold plug tobacco at greatly reduced prices. Its leading fighting brand bore the appropriate name of "Battle Ax." At one time this brand was sold to jobbers as low as 13 cents per pound, which, considering the revenue tax, was below the cost of production. The company's immense profits from its cigarette business furnished the means for conducting this expensive competitive struggle, in which

several millions were sacrificed. The American Tobacco Company's plug business increased swiftly, and by 1897 it had more than one fifth of the total plug output of the country. To enable the company to fill its orders, an additional plug plant was purchased in 1895, and another erected.

THE PLUG-TOBACCO COMBINATION, 1898–1899

By 1898 a number of the leading independent manufacturers of plug tobacco had wearied of the fierce competitive struggle and were prepared to consider propositions for combining their interests with those of the American Tobacco Company. The first negotiations, early in 1898, were, however, unsuccessful, partly by reason of the increase in taxes during the Spanish-American war, which appeared to the financiers who were promoting the enterprise likely to interfere with its profitableness. Shortly thereafter the American Tobacco Company bought outright two important plug-manufacturing concerns — the Brown Brothers and Drummond tobacco companies, of St. Louis. This greatly strengthened the position of the American, and it apparently determined to renew the vigorous competition of the preceding years against its powerful rivals. For this purpose the price of "Horseshoe," the leading brand of the Drummond concern, was sharply reduced.

Before this new competitive fight had become very active, however, further negotiations for combination began. The plug combination, known as the Continental Tobacco Company, was organized on December 10, 1898. It took over the plug business of the American Tobacco Company, including the Brown and Drummond concerns, and also that of six leading competitors, while a few months later the most important competitor of all, the Liggett & Myers Tobacco Company, was also brought into the combination. Several of the concerns acquired had also a large business in smoking tobacco. Although the American Tobacco Company did not at that time own a majority of the stock of the Continental Tobacco Company, the men connected with the American were, from the very first, dominant in the Continental's directorate.

The Continental Tobacco Company issued at the time of its organization $62,290,700 of stock. This amount was still further increased in April, 1899, by reason of the acquisition of the Liggett & Myers concern. The total issue then became $48,844,600 of preferred stock and $48,846,100 of common stock, or $97,690,700 altogether, an amount which thereafter remained unchanged. The company was greatly overcapitalized, the common stock being issued wholly as a bonus. Much the greater part of both classes of stock was given directly in exchange for the property and business acquired. The company issued $15,137,100 of preferred and a like amount of common stock for the property and business turned over by the American Tobacco Company; $17,500,000 each of preferred and common for $5,000,000 in cash and the property and business of the Liggett & Myers Tobacco Company; and $13,456,100 in preferred and $16,207,500 in common stock for the property and business of other concerns. From the beginning the American Tobacco Company had complete control over the new combination.

Entrance of Financiers into the Management

The acquisition of the Liggett & Myers Tobacco Company by the Continental, just referred to, was part of a series of transactions which had a most important influence upon the personnel of both the American and Continental tobacco companies. During 1898 a group of powerful financial interests, including Thomas F. Ryan, P. A. B. Widener, A. N. Brady, W. C. Whitney, and Thomas Dolan, bought up the Blackwell's Durham Tobacco Company, an important manufacturer of smoking tobacco, and the National Cigarette and Tobacco Company, combining them under the name of the Union Tobacco Company. They also secured an option upon a controlling portion of the stock of the Liggett & Myers Tobacco Company, control of which of course was very important to the new plug combination. Mr. Duke and his associates in the American and Continental companies realized the seriousness of the possible competition of the Union Tobacco Company interests, backed by these wealthy financiers. They therefore entered into

negotiations with these financiers and bought out the properties they controlled at a high price. In the spring of 1899 the assets of the Union Tobacco Company proper were taken over by the American Tobacco Company in exchange for $12,500,000 common stock. Shortly afterwards, through another syndicate, composed in part of the men above mentioned, but also including J. B. Duke, O. H. Payne, and H. D. Terrell, the Liggett & Myers Tobacco Company assets, together with $5,000,000 in cash, were transferred to the Continental Tobacco Company in exchange for $17,500,000 of its common stock and $17,500,000 of preferred stock.

These transactions were important, not only because they still further inflated the capitalization of the two companies, but because they resulted in giving a very large stock interest in both to the financiers who had organized the Union Tobacco Company. Most of these men shortly thereafter entered the directorate of either the American or Continental company, or both, and from that time on have been important factors in the control of the entire Tobacco combination.

Already before this time there had been marked changes in the directorate of the American Tobacco Company. The campaign for control of a larger part of the tobacco industry, which has just been recounted, had not been favored by most of the leaders in the original cigarette combination. Consequently, Ginter, Kinney, Kimball, and Emery (owner of Goodwin & Co.) had practically disposed of their interests in the American Tobacco Company by the spring of 1898. Indeed, none of them was a director in that company after the spring meeting of 1897.

This defection of most of the large stockholders among those who had organized the original combination found other men, possessed of large capital but without previous experience in tobacco manufacture, ready to avail themselves of the opportunity offered. During the latter part of 1897 and early in 1898 Oliver H. Payne and H. L. Terrell invested freely in stocks of the American Tobacco Company and were elected directors. At about this time Moore & Schley, New York bankers and brokers, also established close relations with the combination. They financed the organization of the Continental Tobacco Com-

pany. These new men, together with those who entered the management as the result of the Union Tobacco Company transaction, have had a powerful influence in the subsequent expansion policy of the combination, both by furnishing capital and in other ways.

At the time of the purchase of the Union Tobacco Company the American Tobacco Company paid, out of its accumulated surplus and the profits of the sale of its plug business to the Continental, a stock dividend of 100 per cent, or $21,000,000, to its common-stock holders. This, with the stock issued for the Union, added $33,500,000 to the company's capital stock and almost doubled the capitalization already existing. From this time on until 1904 the capitalization of the American Tobacco Company consisted of $54,500,000 of common stock and $14,000,000 of preferred stock.

The Snuff Combination

Within a short time after the organization of the Continental Tobacco Company the combined interests obtained control of practically all the leading snuff concerns of the country. Ever since 1891 the American Tobacco Company had had a small snuff business. The Continental had acquired the extensive snuff business of the P. Lorillard Company, and in 1899 the American Tobacco Company acquired two or three additional snuff concerns. The two companies together had at the beginning of 1900 substantially one third of the snuff business of the country. About two years before this, however, a combination of the important strong Scotch snuff-manufacturing concerns of the country had been effected independently of the American and Continental interests, under the name of the Atlantic Snuff Company. The output of this concern was greater than that of the Continental and American together. During 1899 a vigorous competitive warfare was conducted between these two groups of interests. Early in 1900, however, they came together in the formation of the American Snuff Company, which also took in another important concern, the George W. Helme Company.

The American Snuff Company was organized on March 12, 1900. It issued $12,000,000 of 6 per cent preferred and $11,001,700 of common stock. The American and Conti-

nental interests (including the Lorillard Company) received $10,000,000, the Atlantic Snuff Company interest $10,000,000, and the Helme Company $3,000,000 of the stock. The Atlantic Snuff Company interests, however, obtained three quarters preferred and one quarter common stock, while the American Tobacco Company interests received only one quarter preferred and three quarters common. The common stock was at first considered of much less value than the preferred; but with the growing prosperity of the business arising largely from the almost complete monopoly the common stock has now become the more valuable. It has paid regularly for several years 10 per cent dividends, while the company has also accumulated a large surplus.[1]

The Combination's Control of the Industry in 1900

The organization of the Continental Tobacco Company, the American Tobacco Company's acquisition of the Union Tobacco Company and of other concerns in 1899, and the formation of the American Snuff Company at once raised the Tobacco combination to a dominant position in the manufacture of all the important kinds of tobacco except cigars. In 1900 the combination had 62 per cent of the national output of plug tobacco and 59.2 per cent of the output of smoking tobacco; in 1901, the first full year of the American Snuff Company, it had 80.2 per cent of the output of snuff. In 1897 the American Tobacco Company had controlled barely a fifth of any one of these products. The combination, moreover, still retained substantially a monopoly control over the cigarette business, making 92.7 per cent of the national output in 1900.

The Cigar Combination

Last of all the combination turned its attention to the cigar business, the most important of all the branches of tobacco manufacture, but also the most difficult in which to make an effective combination, because of the immense number of concerns in the trade.

[1] 1908–9, 16 p.c.; then to 1912, 20 p.c. dividends with extras. *Ed.*

Since 1891 the American Tobacco Company had had a considerable business in the manufacture of cheroots, but had made no ordinary cigars. Soon after the organization of the Continental Tobacco Company, however, the American began plans to enter the cigar business. Inasmuch as it had found that its position in the cigarette business had been greatly strengthened by the control of machine patents, it began experimentation with machines for making cigars. Up to the present time, however, machinery has become of comparatively little importance in the manufacture of any but the cheaper types of cigars. Nevertheless, the American Tobacco Company interests in 1901 entered extensively into the cigar business by the organization of the American Cigar Company.

This company, incorporated January 12, 1901, started with an authorized capital stock of $10,000,000, of which $9,965,000 was issued. The Continental and American tobacco companies each took $3,500,000 of the stock. Soon afterwards $10,000,000 of ten-year gold notes were issued by the American Cigar Company, guaranteed by the same two companies. In 1905, $10,000,000 of preferred stock was issued.

The American Cigar Company took over the greater part of the cheroot and small-cigar business of the American Tobacco Company, and proceeded to buy up a number of existing cigar-manufacturing concerns. The most important was Powell, Smith & Co., an arrangement for the absorption of which had been made even before the organization of the American Cigar Company. Another important acquisition was that of the Havana-American Company, a combination which had been established by other interests in 1899 and which controlled an annual output of about 100 million high-grade cigars, chiefly made from Cuban tobacco.

The acquisitions made by the American Cigar Company in 1901 immediately made it the largest single manufacturer of cigars in the country, but it did not then possess, and has never since possessed, any large proportion of the total cigar business of the United States. During the years 1901 to 1903, however, it greatly increased its output, though only at the expense of heavy losses, due to extravagant advertising and schemes and

deals in connection with the American and Continental companies. In 1903 it had about one sixth of the cigar output of the United States.

The new capital made available by the Consolidated Tobacco Company, which was organized soon after the American Cigar Company, was in part used in this expansion of the cigar business.

THE CONSOLIDATED TOBACCO COMPANY, 1901

The Consolidated Tobacco Company, organized in June, 1901, still further cemented the union between the two principal combinations — the American and Continental companies — by acquiring nearly the entire amount of the common stock of both. The Consolidated also gave still more complete control to the few men who were already the leaders in the management and gave them the surplus profits of the business. An immediate object, however, was to secure additional capital for the expansion of the business of the combination, particularly in the cigar industry and in foreign countries.

The Consolidated Tobacco Company had at the outset a capital stock of $30,000,000, which was paid in in cash; this was increased to $40,000,000 at the end of 1902. Immediately after its organization the Consolidated issued a circular, giving the names of its directors, who were mostly men already in the directorates of the other two companies, and offering to exchange its 4 per cent bonds in equal amounts for the common stock of the Continental Tobacco Company, and to exchange them at the rate of $200 for $100 for the common stock of the American Tobacco Company. The offer was promptly accepted by nearly all the stockholders. Ultimately the amount of bonds issued by the Consolidated for this purpose became $157,378,200, with which $54,274,550 of American and $48,829,100 of Continental common stock were acquired. The exchange of a double amount of bonds for the American Tobacco Company stock meant, of course, a still larger overcapitalization as compared with the actual investment.

The owners of the stock of the Consolidated thus acquired effective control of both the American and the Continental, and

became entitled to all the profits of both in excess of the fixed amounts required for dividends on their preferred stocks and for interest on the Consolidated bonds. This exchange of stock for bonds had appeared at the time highly advantageous to the common-stock holders of the American and Continental companies. The Continental common stock had never paid a dividend, and during much of the time had sold at between $20 and $30 per $100 share; the holders were now guaranteed 4 per cent on the par value. The American Tobacco Company's common stock, since the declaration of the 100 per cent stock dividend in 1899, had paid only 6 per cent, and the exchange was equivalent to a guaranty of 8 per cent. The actual earnings of the company were about 9 per cent.

Nevertheless, the transaction actually proved enormously profitable to the men who organized the Consolidated Tobacco Company. Those men had been for the most part in the directorates of the American and Continental companies, and they were in a far better position than most outside stockholders to form a correct judgment as to the probable great increase in profits that was likely to occur in the near future.

The probability of such an increase in profits lay in the changes in the internal-revenue taxes on tobacco products. Those taxes had been greatly increased in 1898, to provide funds for the Spanish war. Already, before the organization of the Consolidated, Congress had passed an act to reduce the tax on "manufactured tobacco" (*i.e.*, chewing and smoking tobacco) and snuff from 12 cents to 9.6 cents per pound and that on cigarettes from $1.50 to $1.08 per thousand (54 cents for cheap grades). This reduction was to take effect on July 1, 1901, or a few weeks after the Consolidated was established. Presumably, also, the directors of that concern foresaw that the tax on manufactured tobacco and snuff would be still further reduced later, to bring it back to the basis which had existed before the war. This actually occurred in 1902, when it was made 6 cents. When the tax had been advanced, the manufacturers of tobacco had barely been able to raise prices sufficiently to recoup themselves; but the men connected with the Consolidated evidently foresaw that prices would not have to be reduced by

an amount at all commensurate with the reduction in the taxes — particularly in view of the large proportion of the business now possessed by the combination and its consequent large measure of control over prices — and that consequently profits would greatly increase.

Such, in fact, proved to be the case. On the basis of the rate of earnings of the American and Continental prior to the formation of the Consolidated, it would scarcely have been possible to pay dividends on their preferred stocks and interest on the Consolidated bonds. During the three years and four months following the organization of the Consolidated, however, the earnings of the two companies were sufficient to pay those charges and also to leave a profit of fully $30,000,000 to the Consolidated on its investment of $30,000,000 (part of the time $40,000,000). That company during this period of time paid $6,000,000 in dividends, accumulated a surplus of $17,000,000, and substantially became entitled also to the increase in the surpluses of the American and Continental Companies, amounting to over $7,000,000.

The benefit in this increase in profits was, by reason of the organization of the Consolidated, largely concentrated in the hands of a few men. This is seen in the fact that immediately after the organization of the Consolidated more than half of its shares were held by six men — James B. Duke, A. N. Brady, O. H. Payne, Thomas F. Ryan, P. A. B. Widener, and William C. Whitney. Through the ownership of the stocks of the American and Continental by the Consolidated, these six men were, moreover, in position to dominate the entire combination. The same six men had just previously owned only a minority of the stocks of the American and apparently very little of the Continental, though they had been very powerful in the management of both. Most of these men, it will be observed, were the financiers who had entered the combination in 1898 and 1899. They and a few associates had supplied the greater part of the new capital now made available for the expansion policy; but they did so only because it was evident that, through the organization of the Consolidated, they might enormously increase their power and their share in the prospective profits of the business.

The British Campaign of the Combination, 1901–2[1]

Combination in the Cuban Cigar Business, 1902

Another direction in which expansion was now sought was in cigar manufacture. Here, too, the new capital furnished by the Consolidated was useful. Aside from the activity of the American Cigar Company in the domestic trade, already referred to, that company now undertook to secure a dominant position in the important cigar business of Cuba.

Early in 1902 it bought two large factories at Havana, combining them under the name of H. de Cabañas y Carbajal (Incorporated). This company issued $1,500,000 of stock, all of which was held by the American Cigar Company. Shortly afterwards, on May 28, 1902, the Havana Tobacco Company was organized. It took over the Stocks of Henry Clay and Bock & Co., and the Havana Commercial Company, two combinations which had been formed by independent interests some time before, and also that of the Cabañas y Carbajal Company. The new corporation issued no less than $30,000,000 of common stock and $5,000,000 of preferred, together with $7,500,000 of bonds. The American Cigar Company received for the $1,500,000 of Cabañas y Carbajal stock $20,000,000 of common stock of the Havana Tobacco Company and $2,625,000 of its bonds. The common stock had little value, except for purposes of control, and has never paid a dividend. The Havana Tobacco Company from the outset controlled a large proportion of the manufacture of cigars in Cuba.

The American Cigar Company also turned its attention to the manufacture of Stogies, a cheap form of cigar. A combination called the United States Cigar Company had already been made by leading stogie manufacturers, independently of the American Cigar Company. In 1903 the American Stogie Company was organized, issuing $976,000 of preferred stock and $10,879,000 of common stock. It took over the assets of the earlier combination, giving for them $976,000 in preferred stock and about $2,500,000 in common stock. The majority of the common

[1] See p. 298, *infra*.

stock, however, was given to the American Cigar Company. The company was enormously overcapitalized, and this stock had little value except for purposes of control, and has never paid a dividend.

Merger in the American Tobacco Company, 1904

The control of the Tobacco combination continued to be exercised through the Consolidated Tobacco Company until October 19, 1904. At that time the Consolidated and its two subsidiary companies, the American and the Continental, were all merged into one company called the American Tobacco Company. This merger was prompted in part by the adverse decision of the Supreme Court of the United States in the Northern Securities case. The Consolidated Tobacco Company was purely a stockholding company, somewhat analogous to the Northern Securities Company. The merger further fortified the dominant position of the men already in control of the Tobacco combination. It also served to simplify the organization and the securities of the combination.

The merger was accomplished by giving the securities of the reorganized American Tobacco Company in exchange for all the securities of the Consolidated, Continental, and old American companies which were in the hands of the public (this term being used to designate all holders except the three big companies themselves), such previous securities being thereupon canceled, and by the direct cancellation of intercompany holdings. The small amount of American and Continental common stock which was in the hands of the public, $242,400, and the stock of the Consolidated Tobacco Company, $40,000,000, were exchanged for an equal amount of common stock of the reorganized American. The preferred stock of the American Tobacco Company, all of which was in the hands of the public, and that part of the preferred stock of the Continental Tobacco Company which was in the hands of the public (about two-thirds of the total), were exchanged for 6 per cent bonds of the reorganized American Tobacco Company on such a basis as to make the return to the holder the same as before. The immense

amount of Consolidated Tobacco Company bonds, $157,378,200, which had been issued against the common stocks of the American and Continental companies, was exchanged dollar for dollar, half for preferred stock of the reorganized American bearing 6 per cent dividends and half for its 4 per cent bonds. The result was that the reorganized American Tobacco Company had outstanding in 1904, $40,242,400 of common stock, $78,689,100 of preferred stock, and $136,360,600 of bonds.

The preferred stock of the new American Tobacco Company was given no voting power for the election of directors or on ordinary matters. The power of the men who had controlled the Consolidated stock was thus made even more secure under the reorganization than it had been during the existence of the Consolidated Tobacco Company, for at that time the preferred stocks of the American and Continental companies, which were largely in the hands of the outsiders, had a voting power, although those stocks were a minority as compared with the common stock held by the Consolidated.

General Policy of Absorption and Domination

The history of the Tobacco combination thus presented shows plainly that the leading purpose of the men who have controlled it has been to dominate the tobacco industry. They started out by practically monopolizing the cigarette business. With the great profits derived from that source they carried on a strenuous competitive fight in the plug industry, which ultimately forced the leading competing manufacturers into combination with themselves. This secured for the combination a dominant position in the manufacture, not only of plug, but of smoking tobacco. Soon after, the combination in the snuff industry was brought about, and subsequently a combination in the cigar industry. The latter, however, controls only a limited proportion of the business.

The successive combinations which these men have established, except that in the cigar business, at the outset took in the leading manufacturers and secured a very large degree of control over the business. That degree of control, however, has been further

extended by the acquisition, either by direct purchase or by securing a controlling stock interest, of a very large number of other competing concerns. The total number of formerly separate concerns and combinations which have passed under the control of the Tobacco combination is in the neighborhood of 250. This number includes the concerns which originally entered the several combinations, but such original acquisitions, though in general they were the largest concerns, were much less numerous than the concerns acquired subsequent to the formation of the combinations. It appears to have been the policy in fact to buy up, from time to time, most competitors whose business had become successful.

The effect of these later acquisitions is best seen in the increase in the proportion of the business controlled. In 1900, shortly after the formation of the Continental Tobacco Company, the Tobacco Company controlled about 60 per cent of the production of chewing and smoking tobacco in the United States. In 1906 it controlled 81.8 per cent of the chewing tobacco and 70.6 per cent of the smoking tobacco. Its proportion of the manufacture of snuff increased from 80.2 per cent in 1901, the first full year of the operation of the American Snuff Company, to 96 per cent in 1906.

A significant feature of many of the acquisitions of the combination, particularly during the period from 1902 to 1904, is the fact that they were made secretly and that the American Tobacco Company interests, as long as possible, concealed their control, continuing to operate the concerns as though independent and often using them as a special instrument for attacking the business of genuine competitors.

Aside from concerns engaged in tobacco manufacture, the American Tobacco Company, and to a less extent the other affiliated combinations, have, particularly since 1899, acquired control of many concerns engaged in enterprises contributory to tobacco manufacture. Concerns thus brought under the control of the combination include many engaged in the wholesale or retail distribution of tobacco products, several producing leaf tobacco in Cuba and Porto Rico, a number which make packages and materials, other than tobacco, used in tobacco manufac-

ture, several which exploit patents for machinery or manufacture machinery for the use of tobacco factories, and a few which handle by-products, make smokers' supplies, etc. The most important of these contributory enterprises of which the combination has secured control is the manufacture of licorice, which is a very important material in tobacco manufacture. Through the MacAndrews & Forbes Company, which has bought up several competing concerns, the American Tobacco Company interests have substantially a complete monopoly of the licorice business.

PRESENT ORGANIZATION AND BUSINESS OF THE TOBACCO COMBINATION

The Four Principal Companies in the Combination

The history of the Tobacco combination has made it clear that the American Tobacco Company has throughout been the principal factor, and this is still more true since the reorganization of 1904, which united the Consolidated, American, and Continental companies under the new corporation with the old name, American Tobacco Company. There are three other corporations still, however, whose position in the Tobacco combination distinguishes them from the great majority of the subsidiary companies. These are the American Snuff Company, the American Cigar Company, and the British-American Tobacco Company.

The American Tobacco Company not only controls the other three principal companies named, but is itself a great manufacturing concern, and it also directly controls a large number of other subsidiary companies. The field of the American Tobacco Company and these subsidiary companies includes the manufacture of chewing and smoking tobacco, of cigarettes for domestic consumption, and of so-called little cigars, together with enterprises contributory to these branches of tobacco manufacture.

The American Snuff Company, with its subsidiary companies, is exclusively concerned with the manufacture of snuff.

The American Cigar Company, with its subsidiaries, handles the cigar business of the combination, including the manufacture of ordinary cigars, cheroots and stogies in the United States and the manufacture of cigars and cigarettes in Cuba and Porto Rico.

The British-American Tobacco Company is distinguished from the others by being confined to export business and to the manufacture and sale of tobacco in foreign countries.

The American Tobacco Company holds considerably more than a majority of the capital stock of the American Cigar and British-American companies and over 40 per cent of the stock of the American Snuff Company. By reason of the fact that certain large individual stockholders of the American Tobacco Company are also stockholders in the American Snuff Company, and by reason of the identity of purposes, the American Snuff Company may properly be considered as controlled by the American Tobacco Company.

The Subsidiary Companies

Aside from these four principal companies, there are 82 other companies in the Combination which do business in the United States, Porto Rico, and Cuba, besides a considerable number controlled by the British-American Tobacco Company, which do business in other countries. In practically every one of these 82 companies a majority of the stock is held either by one of the four principal companies or by some company subsidiary to them. In a large number of cases the entire stock of these subsidiary companies is thus held. The combination in buying stocks has apparently sought control even more than investment.

The American Tobacco Company itself controls directly or indirectly 47 of these subsidiary companies, aside from controlling the three principal subsidiary combinations. The American Snuff Company controls 6 other companies, the American Cigar Company 26, and the British-American Tobacco Company 3 (these 3 companies buy leaf and manufacture tobacco in the United States for export); the British-American also controls many subsidiary companies operating in other countries.

Concentration of Control

The American Tobacco Company, therefore, stands in a controlling position over the entire Tobacco combination with its 86 companies operating in the United States, Porto Rico, and Cuba. The control of the American Tobacco Company itself rests in a very few hands. That company had at the end of 1906 a total capitalization of a little over 235 millions, including bonds, but of this capitalization only about one sixth — namely, the common stock, amounting to a little over 40 millions — has voting power for the election of directors or for the ordinary management of the business. The great bulk of the common stock is held by members of the directorate of the American Tobacco Company and their intimate associates. The 28 directors and 4 other stockholders together own 77 per cent of this stock. Indeed, the ten largest stockholders, 7 of whom are directors, together hold over 60 per cent, and these 10 alone can, therefore, readily dominate the entire combination. They are J. B. Duke (president of the company), A. N. Brady, O. H. Payne, P. A. B. Widener, Thomas F. Ryan, B. N. Duke, G. B. Schley, the banking and brokerage firm of Moore & Schley (chiefly as agents for clients), and the estates of W. C. Whitney and W. L. Elkins.

Capitalization of the Combination

The American Tobacco Company is authorized to issue $80,000,000 of 6 per cent cumulative preferred stock and $100,000,000 of common stock, but only about two fifths of the latter has been issued. The amount of each class of securities outstanding at the end of 1906 was:

Common stock	$40,242,400
Preferred stock, 6 per cent cumulative	78,689,100
Six per cent gold bonds, due 1944	55,208,350
Four per cent gold bonds, due 1951	[1] 61,052,100
Total	$235,191,950

[1] Including $5,010,500 of Consolidated Tobacco Company bonds assumed by the American Tobacco Company.

The total capitalization of all the 86 companies making up the combination in the United States, Porto Rico, and Cuba amounted at the end of 1906 to $450,395,890, consisting of about 130 millions of preferred stock, about 183 millions of common stock, and about 137 millions of bonds. Of this capitalization, however, a large amount is duplicated by reason of the holding of securities in one company by another company in the combination. The total amount thus held is a little over 134 millions (about half a million of which is stock of the American Tobacco Company itself), leaving as the net capitalization in the hands of the public (including the directors and their associates as well as all other holders except companies in the combination) $316,346,821. This latter amount consists of about 103 millions of preferred stock, about 79 millions of common stock, and about 133 millions of bonds. Of the 316 millions of securities in the hands of the public, 235 millions, or about three fourths, consist of the issues of the American Tobacco Company itself. The gross outstanding capitalization of all the other companies is $215,203,940, but of this amount more than 60 per cent, or nearly 134 millons, is held by companies in the Combination.

The Policy of Stock Ownership

The extent to which the Tobacco combination has maintained its control through stock ownership in subsidiary companies, instead of through direct ownership of all plants and other assets, shows that this method of control must possess certain special advantages. This policy of stock ownership has been particularly conspicuous since 1899.

When this policy of stock acquisition was first inaugurated, it was the more common practice of the combination to acquire only a controlling interest in the securities of other corporations, leaving a minority in the hands of the former owners. This practice had various apparent advantages. Through it the Combination was able to acquire control over business without a correspondingly great investment of capital. In some instances it secured stock interests in concerns engaged in contributory

enterprises without investment of capital, but merely in return for contracts for the supply of materials or services to the combination. In numerous cases it appeared advantageous to leave a minority of the stock in the hands of the original owners in order to retain their interest and skill and to take advantage of their personal following among customers. In some cases, moreover, owners of enterprises were unwilling to sell out absolutely, with the consequent result of having either to quit the business or become mere salaried employees, but were willing to transfer a controlling interest to the combination. Even at this time, however, the combination acquired the entire capital stock of certain corporations and retained their separate existence, and recently this has been its prevalent practice. The combination has, in fact, during the past few years, acquired the remaining shares in a considerable number of companies in which it at first held only a controlling interest. Various reasons have led the combination to continue the separate corporate existence of many of the concerns which it thus completely owned. Aside from advantages arising from legal considerations — the avoidance of the necessity of making reports of the business of the parent corporation in compliance with the laws of certain States, economy with respect to corporation fees and taxes, and the like — the continued existence of such concerns has often been highly desirable on account of the trade value of their names.

Secretly Controlled Companies

The most important motive, however, for the continuance of separate corporate existence in the case of many concerns has been the desire of the combination to keep its control secret. There is a strong feeling among many dealers and consumers against "trusts" in general and the "Tobacco Trust" in particular. Independent manufacturers have extensively taken advantage of this feeling and have advertised their goods as "Independent," "Not made by a Trust," and so forth. The attitude of the American Tobacco Company and its openly affiliated concerns in refusing to deal with labor organizations

has also caused hostility among union laboring men, many of whom insist on buying "union-label" goods. Many independent manufacturers have availed themselves of the union-label sentiment to build up a trade.

In order to overcome the effects of the antitrust sentiment and the union-label sentiment, and even to take advantage of them, the Tobacco combination, particularly during 1903 and 1904, secretly acquired a controlling interest in numerous concerns which had been catering to customers who held those sentiments. Such concerns continued to operate under their former management and kept up a pretense of independence and of hostility to the combination. Those which employed union labor continued to do so and advertised the union label. These secretly controlled concerns were, until the facts were disclosed by the Government, a powerful engine of warfare against the genuine independents and were looked upon by the latter as their worst enemy.

Among the concerns of which control was thus secretly acquired and for a greater or less period secretly maintained by the American and Continental tobacco companies are the following:

[21 companies by name omitted.]

The American Tobacco Company Group

The American Tobacco Company itself, as already stated, is a great manufacturing concern, and it also controls directly a large number of subsidiary companies engaged in the same branches of tobacco manufacture or in contributory enterprises, which, with itself, make up what may be called the American Tobacco Company group. The American Tobacco Company has reserved to itself and to these subsidiary companies the manufacture of cigarettes for domestic consumption (including "little cigars") and of plug tobacco, smoking tobacco, fine-cut tobacco, and scrap tobacco. The company has concentrated its own direct manufacture of these tobacco products for the most part in a limited number of very large plants, having closed most of the plants which have from time to time been acquired.

To a considerable degree the company has pursued the policy of specializing individual large plants on a single class of products. There has also been some concentration and specialization of manufacture in the hands of leading subsidiary companies in this group, but in other cases subsidiary corporations have been continued, even though their output was small and considerably diversified, this policy being chiefly pursued in the case of the secretly controlled concerns.

The cigarette and little-cigar business of the American Tobacco Company proper is conducted in nine plants; but two of these, at New York and Richmond, respectively, make nearly its entire direct output of cigarettes; and two others, at Baltimore and Danville, Va., make much the greater part of its output of little cigars. The cigarettes made in plants directly owned by the company are chiefly made from domestic leaf. The company had during 1906 five subsidiary cigarette companies, the greater part of whose aggregate output consists of Turkish cigarettes.

Of the output of plug and twist tobacco by the American Tobacco Company group in 1906, about 104,000,000 pounds were produced in plants directly owned by the parent company, and about 40,000,000 pounds in plants of subsidiary companies. The 104,000,000 pounds were produced in only six plants, and seven eighths of this amount was made in two of them, the Liggett & Myers-Drummond branch, at St. Louis, and the National Tobacco Works, at Louisville. There are ten subsidiary companies manufacturing plug and twist.

The output of fine-cut tobacco controlled by the American Tobacco Company is all produced in factories which also make smoking tobacco, so that the two products may be considered together. Of the total output of about 115,000,000 pounds of these products by the American Tobacco Company group in 1906, nearly one half was made in plants of subsidiary companies. The American Tobacco Company owns directly nine plants which manufacture smoking tobacco, of which five make that product only. The most important of these plants is at Durham, N.C.; it produced nearly 18,000,000 pounds of granulated smoking tobacco, principally Duke's Mixture, in 1906. The other directly owned plants making smoking tobacco are

located at Baltimore, Louisville, St. Louis, Chicago, Richmond, New York, and New Orleans. Seventeen of the subsidiary companies make more or less smoking tobacco and fine cut, but only five are of much importance. The largest output is that of P. Lorillard Company, of Jersey City. The next largest is that of the Blackwell's Durham Tobacco Company, of Durham, N.C.

The American Tobacco Company group also has a large output of scrap tobacco, which, although classed by the Bureau of Internal Revenue with smoking tobacco, is chiefly used for chewing. By far the larger part of the output of this product however, is in the hands of four subsidiary companies, the most important of which are the Luhrman & Wilbern Tobacco Company, of Middletown, Ohio, and the Day and Night Tobacco Company, of Cincinnati. The control of the latter was at first kept secret, as was that of the Pinkerton Tobacco Company, another manufacturer of scrap. Spaulding & Merrick also make scrap.

The importance of the American Tobacco Company and its directly subsidiary companies as manufacturers of tobacco products may be judged from their total consumption of leaf tobacco, which amounted to nearly 281,000,000 pounds in 1906. The extent to which the Combination has concentrated its manufacture in large plants is seen in the fact that one plant, the Liggett & Myers-Drummond branch at St. Louis, consumed nearly one fifth of this leaf tobacco, while six plants together consumed over 55 per cent of the total, and the twelve largest over 75 per cent. The American Tobacco Company has an extensive leaf department for the purchase, drying, stemming, and storage of leaf tobacco.

The American Tobacco Company is also engaged in numerous contributory enterprises connected with tobacco manufacture. To some extent certain of these, such as the manufacture of packages, are conducted in the same plants which manufacture tobacco, but for the most part they are carried on in other plants and by separate subsidiary companies.

The greatest of these contributing concerns is the MacAndrews & Forbes Company, which has an almost complete monopoly of

the manufacture of licorice paste in the United States. Licorice, next to leaf tobacco, is the most important raw material used in tobacco manufacture, and more than nine tenths of the licorice made in the country is used in tobacco. The MacAndrews & Forbes Company has absorbed several other formerly independent concerns, and now not only furnishes licorice to the American Tobacco Company and its affiliated concerns, but also to most independent tobacco manufacturers. The prices which it charged to the latter were the subject of much complaint, and the company, along with the J. S. Young Company, which it afterwards absorbed, was convicted in the Federal courts of a violation of the Sherman antitrust act.

Other important contributory concerns controlled by the American Tobacco Company are the Conley Foil Company and the Johnston Tin Foil and Metal Company, makers of tinfoil; the Golden Belt Manufacturing Company, maker of cotton bags for packing tobacco; the Mengel Box Company and its two subsidiary concerns, makers of wooden boxes; the American Machine and Foundry Company, the New Jersey Machine Company, and the International Cigar Machinery Company, all of which make machinery or hold and develop patents therefor; the Kentucky Tobacco Product Company, which makes nicotine extracts of various kinds out of tobacco stems, the principal by-product of tobacco manufacture; and the Manhattan Brier Pipe Company.

The American Tobacco Company is also interested in a number of distributing companies, most of which, however, sell not only its own products but also cigars and the products of other branches of the combination, as well as of independent concerns. The most important of these concerns is the United Cigar Stores Company of New Jersey, which has several subsidiaries. This company and most of its subsidiaries operate chains of retail stores, the aggregate number being about four hundred.

Other distributing concerns in which the American Tobacco Company has a stock interest are the Crescent Cigar and Tobacco Company, of New Orleans, and Acker, Merrall & Condit, wholesale and retail grocers of New York; about one fifth of the stock of the latter company is held by the American.

The American Tobacco Company also controls the Thomas Cusack Company, a bill-posting concern, and the Florodora Tag Company, which is at present inactive, but which formerly did an immense business in the distribution of premiums.

Aside from distributing concerns controlled by stock ownership, the American Tobacco Company and its affiliated combinations have very close relations with many other distributing concerns. One method of establishing such relations is by granting special discounts to large jobbing concerns. The smoking-tobacco department of the American Tobacco Company alone paid in 1906 and 1907 special commissions to more than 250 jobbers. Such special commissions are not at the present time in any case conditional upon exclusive distribution of the American Tobacco Company's products, nor, except in cigars, does any jobber have the exclusive right to the wholesale distribution of the products of the combination in any particular territory. To the Metropolitan Tobacco Company, however, the American Tobacco Company has given exclusive control of the wholesale distribution of its products in Greater New York. Subsidiary companies of the Metropolitan control a large part of New Jersey in the same way. The National Cigar Stands Company, which operates cigar stands in a very large number of drug stores scattered throughout the United States, as well as some fifty or sixty leading jobbing concerns, has credits and loans of considerable amount extended to it by the combination. In some cases these credits are of such amount as to give the combination substantial control of the business.

THE SNUFF GROUP

The American Snuff Company and its subsidiary companies are engaged exclusively in the snuff business. The parent company has outstanding $12,000,000 of preferred stock and $11,001,700 of common stock. The American Tobacco Company, together with the P. Lorillard Company, which it controls, owns $2,366,400 of the preferred and $7,500,800 of the common stock, or 42.9 per cent of the entire issue of both com-

bined. Although this is a minority of the stock, the American Snuff Company is as essentially a part of the one great Tobacco combination as the American Tobacco Company itself.

The American Snuff Company has closed up most of the plants which from time to time it has acquired from formerly independent concerns. In 1906 it operated directly four plants and controlled six subsidiary companies; the latter, however, were virtually little more than branches, the entire stock of each being held by the parent company. The directly owned plants produced over three fifths of the output controlled by the combination and the subsidiary companies all of the remainder, except 24,391 pounds made on royalty by the Irby branch of the American Tobacco Company. The directly owned plants are, in the order of their importance, the Helmetta (New Jersey) branch, the Baltimore branch, the Nashville branch, and the Clarksville (Tenn.) branch. The most important subsidiary companies in 1906 were W. E. Garrett & Sons, of Yorklyn, Del., and Weyman & Bro., of Chicago. These companies have since transferred their property directly to the American Snuff Company. W. E. Garrett & Sons in 1906 produced more snuff than any branch directly owned by the American Snuff Company except that at Helmetta, N. J. The next largest of the subsidiary concerns is the Standard Snuff Company, of Nashville; the others — the De Voe Snuff Company, Skinner & Co., and H. Bolander (Incorporated) — are very small concerns.

The Cigar Group

The business of the American Cigar Company and its subsidiary manufacturing concerns in the United States is exclusively the production of cigars, including cheroots and stogies. In Cuba and Porto Rico this group of companies makes both cigars and cigarettes.

The American Cigar Company has outstanding $10,000,000 of preferred stock, $10,000,000 of common stock, and $10,000,000 of ten-year gold notes. The American Tobacco Company holds $8,970,000 of the preferred stock (besides $500,000 held by the American Snuff Company) and $7,725,100 of the common stock.

The output of plants operated directly by the American Cigar Company is confined almost exclusively to ordinary cigars made from domestic leaf and to cheroots. It had 29 plants in operation in 1906, and their aggregate output was about five times as great as the output of cigars by all its subsidiary companies operating in the United States. Most of these 29 plants have been acquired from formerly independent concerns, and many others so acquired have been closed. The two plants at Jersey City and Richmond are the largest in the country, making about 190 million cigars each in 1906.

The American Cigar Company holds the entire capital stock of the Havana-American Company, which is the most important manufacturer of cigars made from Cuban leaf in the United States. This company operates 10 factories, most of them at Key West and Tampa, Fla. The American Cigar Company also holds about three fifths of the stock of the American Stogie Company, a heavily overcapitalized combination of stogie manufacturers (common stock $10,879,000, preferred $976,000). This is a New Jersey corporation, but most of its business has been carried on through a subsidiary Pennsylvania company of the same name (changed in 1907 to Union American Cigar Company), which has recently announced its intention of manufacturing ordinary cigars as well as stogies.

The American Cigar Company controls its important business of manufacturing cigars and cigarettes in Cuba through the Havana Tobacco Company, a greatly overcapitalized concern (common stock $30,000,000, preferred $5,000,000, bonds $7,500,000), nearly half of whose stock is held by the American Cigar Company. This company controls several others — Henry Clay and Bock & Co., Havana Cigar and Tobacco Factories, Havana Commercial Company, H. de Cabañas y Carbajal, and J. S. Murias y Ca. — which together have a considerable proportion of the manufacture of cigars and cigarettes in Cuba.

The American Cigar Company further controls, jointly with the American Tobacco Company, the Porto Rican-American Tobacco Company (capital stock $1,999,000, scrip $72,538), which is much the largest manufacturer of cigars and cigarettes in Porto Rico. It is likewise interested either directly or indi-

rectly in several companies which grow or handle tobacco leaf in Cuba and Porto Rico.

The American Cigar Company has also controlling stock interests in a dozen or more wholesale or retail distributing companies, most of which handle other tobacco products as well as cigars.

British-American Tobacco Company

The British-American Tobacco Company, which is the representative of the Tobacco Combination in export and foreign trade, is an English corporation. It has outstanding $7,290,000 of preferred stock and $18,079,302 of common stock. The American Tobacco Company holds substantially two thirds of each class, namely, $4,860,000 of preferred and $11,897,255 of common. Practically all the rest of the stock is held by the Imperial Tobacco Company, the great British combination.

The principal business of the British-American Tobacco Company in the United States is the purchase and preparation of leaf tobacco for shipment to its affiliated concerns abroad, and the manufacture of cigarettes for export. Its cigarette manufacture is chiefly conducted in one plant at Durham, N. C., but it has also a cigarette plant at Petersburg, Va. The company also controls three subsidiary concerns doing business in the United States.

DEVELOPMENT OF THE COMBINATION'S CONTROL OF THE TOBACCO INDUSTRY

The Combination's Proportion of the Business, 1906

The Tobacco Combination, including the American Tobacco Company and the affiliated combinations and subsidiary companies, occupies a strikingly dominant position in the manufacture of all forms of tobacco, except cigars, in the United States. The table on the opposite page shows its proportion of the output during 1906.

While the Combination manufactures less than one sixth of the cigars made in the United States, it has substantially four fifths of the combined business in other classes of the tobacco

THE COMBINATION'S PROPORTION OF THE OUTPUT OF TOBACCO PRODUCTS, 1906.

Product	Output of United States	The Combination		Independent Concerns	
		Output	Per cent of total	Output	Per cent of total
	Number.	*Number.*		*Number.*	
Cigarettes . . .	6,437,692,637	5,309,128,300	82.5	1,128,564,337	17.5
Little cigars . .	989,751,253	804,433,750	81.3	185,317,503	18.7
Cigars	7,147,548,312	1,052,805,858	14.7	6,094,742,454	85.3
	Pounds	*Pounds*		*Pounds*	
Plug and twist .	182,343,364	149,119,539	81.8	33,223,825	18.2
Smoking . . .	175,672,171	124,032,420	70.6	51,639,751	29.4
Fine cut . . .	12,742,345	10,310,960	80.9	2,431,385	19.1
Snuff	23,518,549	22,576,722	96.0	941,827	4.0
Total manufactured tobacco and snuff . .	394,276,429	306,039,641	77.6	88,236,788	22.4

products, its proportion ranging from 70.6 per cent of the total output in the case of smoking tobacco to 96 per cent in the case of snuff. Combining those products which are measured in pounds — namely, chewing tobacco, smoking tobacco, fine-cut tobacco, and snuff — the Combination's proportion of the output is 77.6 per cent. The Combination has, therefore, very strong monopolistic power.

With the exception of cigarettes, very nearly the entire quantity of manufactured tobacco products made in the United States is consumed there, so that the Combination's proportion of the domestic trade in these products corresponds substantially to its proportion of the entire output. In the case of cigarettes approximately one third of the number made is exported. The Combination has practically the entire export trade, from which it follows that its proportion of the production for domestic consumption is somewhat less than appears in the above table, being 74.5 per cent in 1906.

Conclusion

These facts [Ten pages of detail omitted.] emphasize the conclusion already drawn from the history of the organization of the Tobacco Combination, that its primary object has been to

secure a dominant position in the tobacco business of the United States with the result that it has a nearly complete control of it, save only in the manufacture of cigars.

The combination has superior advantages over competitors, from the great size of its plants and from the control of more efficient machinery. These advantages, however, have not been sufficient to enable it, while charging high prices for the greater part of its product, to increase its degree of control, particularly in view of the fact that many consumers prefer to patronize independent concerns. Despite enormous expenditures for advertising and in "schemes" and despite frequent price cutting by means of its so-called "fighting brands" and its bogus independent concerns, there has been, in several branches of the industry, a constant tendency for competitors to gain business more rapidly than the combination and thus to reduce its proportion of the output. This tendency has been overcome only by continued buying up of competitive concerns. Many weaker concerns have been virtually driven out of business or forced to sell out to the combination, either by reason of the direct competition of the latter, or as an indirect result of the vigorous competition between the combination and larger independent concerns. In the case of the larger and more powerful concerns which it acquired, however, the combination has usually secured control only by paying a high price. The immense profits of the combination have enabled it to keep up this policy.

HISTORY OF THE FOREIGN INTERESTS OF THE TOBACCO COMBINATION[1]

Early History

From the time of the original formation of the American Tobacco Company in 1890 it had a considerable foreign business. For a few years this business consisted chiefly of cigarettes, and was handled directly by the American Tobacco Company itself. As early as 1894, however, several subsidiary

[1] Report U. S. Bureau of Corporations, on the Tobacco Industry, vol. I, Feb. 15, 1909, pp. 165–176.

companies had been organized in Australia (see p. 70), and in the following year several Canadian concerns were combined in the American Tobacco Company of Canada. (See p. 70.) No other important subsidiary corporations were organized or acquired in foreign countries until 1899. In that year, as already related (see p. 83), the American Tobacco Company acquired a controlling interest in a large cigarette-manufacturing business in Japan. Two years later the interests of the company in foreign corporations were extended by the purchase of two thirds of the capital stock of the George A. Jasmatzi Company (Limited), of Dresden, Germany. (See p. 88.)

No exact figures are available as to the output of the above-mentioned foreign concerns, but in 1901 President Duke estimated the output of the Canadian concerns at about 100,000,000 cigarettes annually and that of the Australian factories at about 200,000,000 a year. He said at the same time that the daily production of the Japanese company was 8,000,000 cigarettes. It was reported in the Commercial and Financial Chronicle that the daily production of the German company was 3,000,000 cigarettes, which would amount to over 900,000,000 annually.

In addition to the foreign business handled through the ownership of a controlling interest in these foreign factories, the American Tobacco Company was the principal exporter of cigarettes from the United States. Its exports during its first year in business amounted to only 262,681,500 cigarettes, but they increased steadily and rapidly until the year 1898, when they amounted to 1,215,632,000. In 1890 this export business was a little over one tenth of the entire cigarette output of the American Tobacco Company, and in 1898 very nearly one third. During this period the exports of cigarettes from the United States by all other manufacturers combined were much less than those of the American.

Competitive Campaign of the American Tobacco Company in England

Declining Profits on Exports to England.—In addition to the subsidiary manufacturing corporations referred to above, com-

panies and agencies which operated simply as selling or distributing concerns were established in various countries. One of the most important of these was the London depot of the American Tobacco Company. In 1898 the sales of this depot amounted to $916,729.93, but as the total expenses of the depot, including cost of goods, were $916,732.07 the enterprise was by no means as satisfactory as might have been desired. From that year the sales of the depot declined in amount, and by 1900, the last full year of its operation, they were only $591,897.36. The cost of goods and the expenditures of the agency had not declined in like proportion, for they amounted to $646,835.99, showing a loss on the year's business of over $50,000. The American Tobacco Company ascribed this unsatisfactory condition of its English business to the duties on leaf and manufactured tobacco going into England, which were so arranged as to give a considerable degree of protection to the domestic manufacturer.[1] In view of this condition the officers and managers of the American Tobacco Company decided that it was necessary to acquire or establish a manufacturing plant or plants in England if their business was to meet with success in that country.

Purchase of Ogden's (Limited).—The formation of the Consolidated Tobacco Company in June, 1901, provided the necessary means for carrying out the plans of the men at the head of the Tobacco combination in regard to the acquisition of English plants. The entire $30,000,000 capital stock issued by the Consolidated Tobacco Company was paid in in cash and was available in the form of loans for any of the enterprises undertaken by the American and Continental tobacco companies or the American Cigar Company. Shortly after this large fund of new capital became available President James B. Duke, together with W. R. Harris and C. C. Dula, who were officers of the Consolidated and its affiliated companies, went to England for the purpose of carrying out the plan for establishing a large English manufacturing business. They at once began negotiations for

[1] See Statement of James B. Duke to Industrial Commission, report of Commission, vol. XIII, p. 327.

the purchase of Ogden's (Limited), one of the most important tobacco manufacturing concerns in Great Britain. Before the end of September, 1901, they had acquired substantially the whole outstanding stock of the company. The following statement shows the number of the outstanding shares and the percentage of the total acquired by the American Tobacco Company:

	Total Shares of Company Issued	Acquired by American Tobacco Co.	
		Number	Per cent of total issue
Debenture shares	60,000	59,600	99.3
Preference shares	200,000	199,250	99.6
Ordinary shares	350,000	335,200	95.8

The total cost of the shares acquired was $5,347,888.87.

About this time the British Tobacco Company was incorporated under the English law by the officers of the American Tobacco Company, and it was their intention that it should become a holding company for the interests of the Tobacco combination in Great Britain. As a matter of fact, however, the shares in Ogden's (Limited), were taken over directly by the American Tobacco Company, and on December 31, 1901, that company still held the nominal outstanding stock of the British Tobacco Company, amounting to only £15. Subsequent events prevented the development of this holding company.

Organization of the Imperial Tobacco Company. — The purchase of Ogden's (Limited) caused immediate alarm among the British manufacturers of cigarettes and tobaccos. They feared the power of the American Tobacco Company, with its enormous business and resources. The American scarcely had time to show its policy in the management of the Ogden's concern before the other leading manufacturers of tobacco in Great Britain had formed a combination to resist this dangerous rival.

Thirteen of the largest manufacturers in Great Britain combined to form the Imperial Tobacco Company (of Great Britain and Ireland) (Limited). This company, which was registered

December 10, 1901, amalgamated the tobacco business of the following firms: W. D. & H. O. Wills, Edwards, Ringer & Bigg, and Franklyn, Davey & Co., of Bristol; Lambert & Butler, Hignett's Tobacco Company, and Adkin & Sons, of London; John Player and Sons, Nottingham; Hignett Bros. & Co., William Clarke & Son, and Richmond Cavendish Company, of Liverpool, and Stephen Mitchell & Son, F. & J. Smith, and D. & J. MacDonald of Glasgow. Preliminary agreements for the formation of this combination, which had been made on October 3 and 10, 1901, were ratified by the company on February 3, 1902. The authorized capital was £15,000,000, with additional debenture stock, limited in amount to 50 per cent of the cumulative preference shares for the time being issued, the total limit being £2,500,000. Thus the authorized share and loan capital together was £17,500,000. This was divided as follows:

4½ per cent debenture stock	£2,500,000
5½ per cent cumulative preference shares	5,000,000
6 per cent noncumulative preferred ordinary shares	5,000,000
Deferred ordinary shares	5,000,000
Total capital	£17,500,000

The total capital stock, the amount of each kind of stock issued, and the amounts issued to the vendors and to the public are shown in the table below:

	To Vendors	To the Public	Total Issue	Unissued
Debenture stock	£500,000	£1,000,000	£1,500,000	£1,000,000
Cumulative preference shares	1,500,000	3,000,000	4,500,000	500,000
Preferred ordinary shares	4,259,049	—	4,259,049	740,951
Deferred ordinary shares	4,259,048	—	4,259,048	740,952
Total	£10,518,097	£4,000,000	£14,518,097	£2,981,903

The first column shows that the stock taken by the members of the various firms which combined to form the Imperial Tobacco Company amounted to £10,518,097. They also received £1,438,925 in cash.

The principal items of the assets of the Imperial Tobacco Company, as set forth in its first balance sheet, were:

Land, buildings, plant, machinery, stock, etc., obtained from combining concerns	£3,438,925
Cash, obtained as working capital by sale of stock to the public (in addition to cash paid venders)	2,561,075
Good will	8,518,097
Total	£14,518,097

The average annual profit of the companies combined during the preceding three years was certified to have been £1,062,922, after allowing for depreciation. This, after paying interest on debenture stock and dividends on cumulative preference shares, would equal nearly 9 per cent on both issues of ordinary stock.

An agreement was made by the Imperial Tobacco Company early in its career (January, 1902) with Salmon & Gluckstein (Limited), a corporation manufacturing tobacco and also controlling a number of retail stores in England. Under this agreement the existing £450,000 of the ordinary shares in the latter company were to be converted into 10 per cent preference shares, the dividend to be guaranteed by the Imperial Tobacco Company, and £100,000 in ordinary shares were to be created and issued and to be subscribed for by the Imperial Tobacco Company. This step assured the Imperial Tobacco Company the coöperation of the largest English retail house in its campaign against the American interests.

The Imperial Tobacco Company immediately began a campaign of active competition to check and frustrate the plans of the American Tobacco Company for strengthening its foothold in Great Britain. In March, 1902, the Imperial offered large bonuses to customers who would undertake not to sell American goods for a term of years. The American Tobacco Company, through the Ogden's Company, met this by offering to its British customers, for the next four years, its whole net profits on British business, and £200,000 a year besides. The offer was as follows:

Commencing April 2, 1902, we will for the next four years distribute to such of our customers in the United Kingdom as purchase

direct from us our entire net profits on the goods sold by us in the United Kingdom. In addition to the above, we will, commencing April 2, 1902, for the next four years, distribute to such of our customers in the United Kingdom as purchase direct from us the sum of £200,000 per year. The distribution of net profits will be made as soon after April 2, 1903, and annually thereafter, as the accounts can be audited, and will be in proportion to the purchases made during the year. The distribution as to the £200,000 per year will be made every three months, the first distribution to take place as soon after July 2, 1902, as accounts can be audited, and will be in proportion to the purchases during the three-months period. To participate in this offer we do not ask you to boycott the goods of any other manufacturer.

This offer had a marked effect in opening the British trade to American competition. As a countermove the Imperial Tobacco Company threatened to invade the American market, and in the summer of 1902 it was reported to be selecting sites for factories in this country. Before any definite steps were taken, however, to carry out this plan, an agreement was arrived at between the two great rival corporations which completely changed their position toward each other.

Agreement with the Imperial Tobacco Company

The agreement between the American Tobacco Company interests and the Imperial Tobacco Company was made on September 27, 1902, about a year after the purchase of Ogden's by the American and about seven months after the complete establishment of the Imperial. The agreement was embodied in two documents. The first related to the trade in the United Kingdom and the United States, providing for the transfer of Ogden's to the Imperial and for division of territory between the Imperial and the American. The second provided for the establishment of a new corporation, to be jointly controlled by the American and the Imperial, which was to do business in countries outside of the United Kingdom and the United States.

The former agreement was executed by Ogden's (Limited), the American Tobacco Company, Continental Tobacco Company, American Cigar Company, Consolidated Tobacco Com-

pany, and the British Tobacco Company (Limited), on the one hand, and the Imperial Tobacco Company on the other. By it, Ogden's (Limited) agreed to convey to the Imperial company its whole undertaking clear of incumbrances, except its export business, and except its cash and book accounts. The plant, including land and buildings, machinery, tools, and live stock, was to be taken at the valuation at which it then stood on the books of the Ogden's Company; stock in trade and materials were to be taken at cost; and the Ogden's Company was to receive £1,500,000 for its good will, patents, and trade-marks in ordinary shares, half preferred (6 per cent noncumulative) and half deferred, of the Imperial company. For the tangible assets one third was to be paid in preference shares ($5\frac{1}{2}$ cumulative) of the Imperial, one third in its debenture stock ($4\frac{1}{4}$ per cent) and one third in cash; but if the one third should exceed £300,000, the Imperial company was not required to pay more than that amount in preference shares, but might pay half the excess in additional debenture stock and half in additional cash. Indirectly these various payments came chiefly to the American Tobacco Company as the chief holder of the Ogden's stock. (See pp. omitted.)

The Imperial Tobacco Company agreed not to engage in the tobacco business in the United States, unless through or in connection with the American company and its allies, except that it retained the right to buy and treat tobacco leaf in the United States for the purposes of its business in the United Kingdom. All the companies affiliated with the American Tobacco Company, parties to the agreement, bound themselves in like manner not to carry on the tobacco business in the United Kingdom, and they added the following:

The said covenanting parties will procure the following directors of some or one of them, namely, James Buchanan Duke, Benjamin Newton Duke, Thomas Fortune Ryan, John Blackwell Cobb, Williamson Whitehead Fuller, William Rees Harris, Percival Smith Hill, and Caleb Cushing Dula, and will respectively use their best endeavors to procure such other directors as shall be required by the Imperial company to enter into a covenant with the Imperial company similar to that referred to in the preceding part of this clause.

By a parallel clause, certain directors of the Imperial Company were excluded from the tobacco business in the United States.

Neither the Imperial company nor Salmon & Gluckstein (Limited) was to "sell or consign any tobacco products to any person, firm, or company within the United States except the American company or persons or companies designated by it"; and the several American companies were not to "sell or consign any tobacco products to any person, firm, or company in the United Kingdom except the Imperial company or persons or companies designated by it." Goods sold by one company to another under this clause were to be paid for at cost plus 10 per cent. The Imperial company was to be appointed sole agent within the United Kingdom for Havana and Porto Rican cigars and cigarettes controlled by the American companies, and the Imperial company was not to handle any other Havana or Porto Rican cigars or cigarettes; and on these goods the Imperial company was to have a commission of 7½ per cent. The Imperial company was to use its best endeavors to promote the sale of such cigars and cigarettes in the United Kingdom, and the American company might not call its endeavors in question so long as it maintained a sale of the Havana cigars and cigarettes included in the agency equal to not less than 72 per cent of the total annual importations into the United Kingdom, duty paid, of cigars and cigarettes made in Cuba, the percentage being based on an average of three years. This percentage was fixed on the assumption that the American companies "control or will shortly control not less than 80 per cent of the aforesaid annual importation." This part of the agreement was subsequently modified.

As a means of maintaining the harmony of interests between the British and American concerns, it was provided that the allottees of the £1,500,000 in ordinary shares of the Imperial company, issued in payment for the good will and trade-marks of Ogden's (Limited) — that is, the American Tobacco Company interests — should not "sell or transfer more than 10 per cent of the said shares within the period of five years from the date of their allotment, if and so long as the present directors of the

Imperial company, or some of them, shall hold not less than £3,000,000 in ordinary shares of the Imperial company."

This agreement for exclusive territory is still in full effect and is strictly observed.

Present Capitalization and Business of the Imperial Tobacco Company. — At the time when the Ogden's purchase was made by the Imperial, in 1902, the Imperial increased its authorized capital from £15,000,000 to £18,000,000, namely, £6,000,000 in preference shares, £6,000,000 in preferred ordinary shares, and £6,000,000 in deferred ordinary shares. By no means all this stock, however, was issued at the time or has since been issued. At the beginning of 1907 the outstanding capital stock of the Imperial, together with its issue of debentures, was as follows:

Preference shares	£4,959,249
Preferred ordinary shares	5,260,469
Deferred ordinary shares	5,270,436
Debentures	2,065,011
Total	£17,555,165

It will be observed that the compromise agreement above described specifically reserved to the Imperial Tobacco Company the right to buy and treat leaf tobacco in the United States for the purpose of its business, though it was prohibited from manufacturing finished tobacco products in this country. The Imperial accordingly maintains its own leaf-buying organization in the United States, most of its raw material coming from this country. It has incorporated this organization under the name of the Imperial Tobacco Company, of Kentucky. It has established its own stemmeries throughout the tobacco districts of Virginia, North Carolina, Kentucky, and Tennessee.

One result of the compromise with the British interests is that several well-known brands of English tobacco which were formerly made only in Great Britain are now made also in the United States to supply the trade here, and thus save the import duty of 55 cents per pound. They bear the same name as before and have the same appearance in every respect, but in small type the packages indicate the fact that the product is made by the American Tobacco Company in this country. There is of course also some English tobacco made by the Imperial in England,

which is sold through the American Tobacco Company or its subsidiaries in the United States.

Profits of the American through the British Campaign

Aside from any advantages which the American Tobacco Company interests secured in the second part of the agreement — that is, in the establishment of the British-American Tobacco Company, as described below — the transfer of Ogden's to the Imperial represented a very considerable profit to the American. The American had paid for its interests in Ogden's (Limited) $5,347,888.87. (See p. 167.) Aside from receiving about $1,570,000, or approximately their original cost, for its holdings of Ogden's debentures and preference shares, the American Tobacco Company became a large holder of ordinary shares of the Imperial through the transfer of the English business of Ogden's to the Imperial. As already stated, £1,500,000, or nearly $7,500,000, was paid by the Imperial for the good will of Ogden's (Limited). Most of this came to the American Tobacco Company as the principal stockholder of Ogden's. The payment was made in the form of 750,000 £1 deferred ordinary shares and 750,000 £1 preferred ordinary shares of the Imperial. Of this stock, 10 per cent was issued to the American Tobacco Company direct, representing compensation to it for the value of its own brands which had been transferred to Ogden's and by it transferred to the Imperial. The remaining 675,000 shares of each class were apportioned among the holders of the ordinary shares of Ogden's (Limited); the American Tobacco Company and its affiliated companies, which held £335,200 out of £350,000 of such ordinary shares, consequently received £646,457 of each class of the Imperial shares for its proportion. The receipts of the American Tobacco Company for its own brands and business and for its interest in Ogden's thus amounted to £721,457 in preferred ordinary stock and an equal amount in deferred ordinary stock, the total par value of these shares in American money being about $7,000,000. This same stock was carried on the books of the American Tobacco Company after the merger in October, 1904.

At the end of 1906 it still held £721,457 of the deferred ordinary shares, but its holdings of the preferred ordinary had fallen to £376,721, large blocks having been sold. At the time when the American Tobacco Company held 721,457 shares each of both the deferred and the preferred ordinary stock of the Imperial its proportion of the total issue of such shares was 13.7 per cent, and its proportion of the entire share capitalization about 8 per cent. By December 31, 1906, this proportion had fallen to about 6 per cent.

The Imperial Tobacco Company has proved very successful, and consequently the ordinary shares received by the American Tobacco Company in exchange for the good will of Ogden's have brought a good return. The total profits of the Imperial were approximately £1,100,000 in 1902, £1,260,000 in 1903, £1,450,000 in 1904, £1,700,000 in 1905, and £1,790,000 in 1906. The deferred ordinary shares, which correspond to common stock, received a dividend of 4 per cent in 1903, 6 per cent in 1904, 8 per cent in 1905, and 10 per cent in 1906. It would appear, therefore, that the securities of the Imperial obtained by the American must be considered to have been worth fully their par value.

The above computation shows over $8,500,000 received by the American Tobacco Company in payment on its interest in Ogden's (Limited). While this is about $3,000,000 in excess of the amount the American paid for Ogden's, it also apparently received shares of the British-American for the good will of the export business of Ogden's. As the accounts of the American Tobacco Company combine these shares with those received for its own export business, the exact amount of either payment has not been ascertained.

Although this transaction was financially profitable to the American Tobacco Company interests, there is little doubt that their campaign in Great Britain fell short in results of what had been anticipated. The American Tobacco men had apparently aspired to substantial domination in the British market. The actual result was the formation of a powerful combination in Great Britain in which the American interests held only a small proportion of the stock.

The agreement, on the other hand, whereby the control of the foreign business of the Imperial and American was combined under the British-American was exceedingly profitable to the American Tobacco Company. In the four years of complete operation of that concern (1904–1907, inclusive), the American received more than $7,000,000 in dividends, while the foreign trade, including investments, in the preceding four years yielded less than $2,000,000.

History of the British-American Tobacco Company

As already stated, the second agreement of September 27, 1902, between the Imperial Tobacco Company and the American Tobacco Company interests provided for the organization of a tobacco corporation to do business outside of those territories specifically reserved to the Imperial Tobacco Company and to the American Tobacco Company and its associated concerns, respectively; that is to say, practically outside of the United Kingdom and of the United States and its noncontiguous territories. This new corporation was known as the British-American Tobacco Company (Limited). (See Exhibit No. 2, p. 440.)

The agreement providing for the establishment of this company was signed by the Imperial Tobacco Company, Ogden's (Limited), the American Tobacco Company, Continental Tobacco Company, American Cigar Company, Consolidated Tobacco Company, and "Williamson Whitehead Fuller and James Inskip, on behalf of a company intended to be formed under the companies' acts, 1862 to 1900, with the name of 'British-American Tobacco Company (Limited).'"

The British-American Company was to buy the export business of the other signatories "and the good will appertaining thereto, to include formulæ and recipes of preparation, treatment, and manufacture, as well as license to use patent rights, trade-marks, brands, licenses, and other exclusive rights and privileges, for the purposes of such export business, and shall also include all stock or shares in companies incorporated in countries foreign to the United Kingdom and the United

States, . . . including all shares of the American Company in Georg A. Jasmatzi Company (of Dresden), and all shares of the Imperial Company in W. D. & H. O. Wills (Australia) (Limited)." The words "United Kingdom" were defined to mean, for the purposes of the agreement, Great Britain and Ireland and the Isle of Man, and the words "United States" to mean "the United States of America as now constituted, Cuba, Porto Rico, the Hawaiian Islands, and the Philippine Islands." The words "export business" were defined to mean:

The manufacture of and dealing in tobacco and its products in any country or place outside the United Kingdom and the United States, and the manufacture of and dealing in tobacco and its products within the United Kingdom for export to any other country except the United States, and the manufacture of and dealing in tobacco and its products in the United States (except in Cuba, Porto Rico, the Hawaiian Islands, and the Philippine Islands), for the purpose of export to any other country except the United Kingdom, and the manufacture and selling in the United Kingdom and the United States, respectively, of tobacco to be supplied to ships in port for the purposes of ships' stores.

For the whole export business, rights, and shares in other companies, to be thus acquired, the British-American company was to issue £2,820,000 in its ordinary shares. One third of this, or £940,000, was to go to the Imperial company, and two thirds, or £1,880,000, to "the Ogden company, the American company, the Continental company, the Cigar company, and the Consolidated company, or some of them, in such proportions as they shall mutually agree." In addition to the shares thus issued, the Imperial company was to take a further amount of £300,000, and the American companies a further amount of £600,000, in the ordinary stock of the British-American, which they were to pay for in cash. The £2,820,000 stock issued for the "export business" was given for good will and other intangible assets; it did not include the export factories nor stock in trade. These were to be separately paid for in cash (out of the proceeds of the cash stock subscription), the factories and equipment at the values at which they stood on the books of the vendors and the stock in trade and materials at cost.

The British-American company agreed not to engage in "the business of a tobacco manufacturer, or in any dealing in tobacco or its products, except in the manner and within the limits contemplated and authorized by this agreement," and each of the other companies agreed not to engage in export business, as defined in the agreement, except as it might be interested as a member of the British-American company or of a company formed with its concurrence, and also except so far as the American companies might be interested as members of companies or firms engaged in exporting cigars and cigarettes from Cuba, Porto Rico, the Hawaiian Islands, and the Philippine Islands.

In pursuance of this agreement the British-American Tobacco Company was incorporated under the laws of Great Britain. Its authorized capital is £6,000,000, £1,500,000 in 5 per cent cumulative preference shares and £4,500,000 in ordinary shares. Only ordinary shares were at first issued. The amount issued in pursuance of the terms of the agreement, as above set forth, was £3,720,021, which was still the amount of ordinary shares outstanding at the end of 1906. Of this, as provided by the agreement, two thirds went to the American Tobacco Company and its affiliated concerns and the remainder to the Imperial Tobacco Company. At the time of the consolidation of the American, Continental, and Consolidated companies, in 1904, the entire amount of ordinary shares of the British-American which had been acquired by them, £2,480,012 ($12,052,858.32), was transferred to the reorganized American Tobacco Company. In 1906 the American Tobacco Company sold 105,333 shares of this stock, its holdings at the end of that year amounting to £2,447,995 ($11,897,255.29).

Some time after the issue of the ordinary shares the entire authorized amount of preference shares, £1,500,000, was issued by the British-American company, precisely two thirds being subscribed by the American Tobacco Company interests and the remainder by the Imperial. The same 1,000,000 shares of preference stock obtained at this time are still held by the American Tobacco Company, the par value in American currency being $4,860,000. These preference shares were paid for

in cash and the proceeds used for developing the business of the British-American.

The total issued capital of the British-American at the end of 1906 was, therefore, £5,220,021 ($25,369,302.06), of which nearly two thirds was held by the American Tobacco Company.

The British-American Tobacco Company has very considerably extended the already large export business which was turned over to it by the American and Imperial companies. (See p. 305.) It manufactures large amounts of tobacco in the United States for export, and it also manufactures some in foreign countries. To a very large extent it acts as a wholesale distributor of its own products and, to some extent, of products purchased from other concerns, particularly from the Imperial and from the American Tobacco Company and its subsidiary concerns. The business of the British-American Tobacco Company is in part carried on in its own name and in part by means of subsidiary companies. Aside from the subsidiary companies in several foreign countries, whose stocks were turned over to the British-American by the American and Imperial interests, it has acquired stocks in a large number of other concerns, both in the United States and foreign countries.

PRICES, COSTS, AND PROFITS[1]

The principal facts shown in this report are grouped below under three heads according as they relate to the combination, to the successor companies, or to other companies.

Combination

The combination originated in 1890 with the formation of the American Tobacco Company, which, through the expansion of its business and the affiliation of numerous other concerns, acquired

[1] Report of U. S. Commissioner of Corporations on the Tobacco Industry, Part III, pp. 1–29, condensed without indicating omissions. This report deals with the results under combination and for the two years, 1912–1913, which succeeded dissolution by the Supreme Court decree (Chapter XVII, *infra*).

a dominating position in the tobacco industry. This combination was dissolved by judicial decree in 1911.

The salient points brought out in this part of the report relative to the business of the combination, so far as it was engaged in the manufacture and sale of tobacco in the United States, are as follows:

(1) That the combination from 1902 to 1910 had a monopolistic position in each of the chief branches of the tobacco business, except in cigars, the minimum proportion of the annual output in the several branches ranging from two thirds to over five sixths of the total output of the country, while in cigars the maximum proportion in any year was only one sixth of the total.

The combination's proportions of the annual output, by branches, from 1902 to 1910 were:

Year	Plug	Smoking	Fine Cut	Snuff	Cigarettes	Little Cigars	Cigars
	Per cent	*Per cent*	*Per cent*	*Per cent*	*Per cent*	*Per cent*	*Per cent*
1902	71.2	66.3	73.7	85.9	84.6	71.8	14.3
1903	76.9	67.1	77.6	89.4	83.9	67.9	16.4
1904	78.2	69.2	80.4	90.6	87.7	79.2	13.9
1905	80.7	68.7	81.7	93.8	84.7	78.3	13.3
1906	81.8	70.6	80.9	96.0	82.5	81.3	14.7
1907	80.5	72.4	81.4	95.7	81.7	90.8	14.5
1908	81.9	73.6	79.2	95.7	81.8	88.7	13.0
1909	83.3	75.3	80.1	96.1	83.6	89.0	13.1
1910	84.9	76.2	79.7	96.5	86.1	91.4	14.4

(2) That for the combination high rates of profit have followed monopolistic control, the greater the degree of control the greater the rate.

Thus, in the plug branch from 1893 to 1898 the combination lost an average of 3 cents per pound of plug tobacco sold. Its output during this period was less than 25 per cent of the total output of the United States. By 1900, however, it had secured 62 per cent of the output and in this year its profit was 3.8 cents per pound, and by 1905 it had secured control of over 80 per cent of the country's output and its profit was nearly 8 cents per pound.

In the smoking branch the combination's control from 1893 to 1898 was less than 25 per cent of the total output of the United States, and its profits averaged about 4 cents per pound. From 1902 to 1910 when the control of the combination was from 66 to 76 per cent its profits were approximately 7 cents per pound.

In the fine-cut branch from 1899 to 1901 the combination's control of the total output was less than 50 per cent. In two of these years it sold its fine-cut product at a loss. On the other hand, from 1902 to 1910 its control was nearly 80 per cent and its profit per pound ranged from 3.9 cents to 7.6 cents.

In the snuff branch the combination had practically a complete control after 1903, and in no other branch were the profits as large or the variations from year to year as small.

In the cigarette branch the combination had practically a complete control from the organization of the American Tobacco Co. in 1890. In this branch the rates of profit were also high, particularly during the earlier years of the combination's existence. The gradual decrease in the profits in the cigarette branch, without any marked decline in its proportion of the total output, was due in part to the fact that it was necessary in order to hold its position to shift during the latter part of the period to newer brands which, on account of the expense of exploitation, afforded a lower rate of return.

In the cigar branch the combination never acquired any large proportion of the business, and the comparative unprofitableness of this branch stands in sharp contrast with the profitableness of the manufactured tobacco, snuff, and cigarette branches in which it had a high degree of control.

It is evident, therefore, that the high rates of profit shown for the combination in those branches in which it had a high degree of control were in great measure due to monopolistic power.

(3) That for most types of manufactured tobacco the combination's rates of profit were ordinarily more than double those of its competitors, though for a few types it had no advantage.

* * * * * * * *

(4) That selling costs were materially reduced as the volume of the combination's business increased.

(5) That generally there were material decreases in advertising expenditures of the combination after a controlling proportion of the total production had been secured.

(6) That there was a large advance in the cost of leaf tobacco for the combination from 1901 to 1910.

(7) That during 1901 and 1902 the internal-revenue tax was reduced 6 cents per pound on manufactured tobacco, 42 cents per thousand on cigarettes, and 46 cents per thousand on little cigars, but the combination made practically no change in the prices to the jobber, while the prices to the consumer also remained unchanged, so that the combination profited by substantially the whole extent of the tax reduction, though it was presumably intended for the benefit of the consumer.[1]

When the rate of internal-revenue tax on tobacco products is increased, one method of adjustment is to reduce the sizes of the package in which tobacco is permitted to be packed. This is for the purpose of enabling the manufacturer to change the sizes of the packages sold at customary retail prices, and in this way to shift the tax increase to the consumer. Thus, in 1898 when the tax on manufactured tobacco was increased from 6 cents to 12 cents per pound, the statutory sizes of package in which most of the tobacco was packed, namely, 2 ounces, 3 ounces, and 4 ounces, were abolished, and 1⅔ ounce, 2½ ounce, and 3⅓ ounce sizes substituted.

In 1901, when the tax was reduced 2.4 cents per pound, the statutory packages of 2 ounces, 3 ounces, and 4 ounces, which had been in vogue prior to 1898, were again permitted to be used, but the tax reduction at this time was not sufficient to enable the combination to supply these larger sizes (if the dealers sold at the customary prices and on their usual margins of profit) without greatly reducing its own profits. The wholesale and retail prices were not changed, therefore, and the combination got the advantage from this reduction in tax. In 1902 the tax was again reduced 3.6 cents per pound, but there was no change in the statutory sizes. The packages of 1⅔ ounces, 2½ ounces, and 3⅓ ounces in which the bulk of the tobacco was

[1] *Cf.* Chapter II, *supra*, on whisky.

then packed were not abolished, but the combination instead of returning to the old larger sizes and thus reducing its prices per pound, which this second tax reduction would have made feasible, continued to supply these smaller sizes at the prices already current. It profited, therefore, by substantially the whole extent of both tax reductions, though Congress presumably intended the reductions for the benefit of the consumer. Similar conditions existed with respect to the tax reductions on cigarettes and little cigars.

(8) That in 1910 when the internal-revenue tax on manufactured tobacco was increased from 6 cents to 8 cents per pound, on cigarettes from $1.08 to $1.25 per thousand, and on little cigars from $0.54 to $0.75 per thousand, the prices of certain products of the combination were increased as much as the tax both to the jobber and the consumer, so that the burden was shifted to the consumer; while for other products the prices to jobbers and consumers were not increased, so that the burden rested on the combination.

In general, prices were increased both to the jobber and to the consumer on brands of smoking and fine-cut tobaccos, but no changes were made in prices to the consumer on plug, snuff, cigarettes, or little cigars, and only small increases were made in prices to the jobber.

The increase in the tax rate per pound was generally a small part of the profit on the more successful brands, and was therefore generally borne by the manufacturers. If they had reduced the quantities in their retail packages for all sizes, they would have generally more than doubled their profits, and apparently they did not regard this as advisable. For smoking and fine cut, in some cases, they reduced the quantity in a package sold at a customary retail price, and in other cases made no change, and thus increased their profits on some sizes and decreased them on others. Taking all kinds of tobacco products together, however, the tax increase in 1910 was largely borne by the combination.

(9) That there were practically no changes in prices to the consumer for the combination's principal brands of manufactured tobacco, cigarettes, and little cigars from 1901 to July, 1910.

(10) That, while there were practically no changes in prices to the consumer from 1901 to July, 1910, for the combination's principal brands, there were substantial increases in prices to jobbers, thus reducing the margins between these prices.

(11) That the most profitable years of the combination's existence were from 1903 to 1908 — the period of low tax, moderate leaf costs, decreased advertising expenditures, and highly monopolistic control.

(12) That the combination for various types or classes of tobacco products developed one or two predominating brands, a policy which tended to promote concentration and economy in manufacture and afforded a greater protection against competition than a multiplicity of brands, but which at the time of dissolution presented difficulties in dividing the business.

Successor Companies

By the term "successor companies" is meant the seven companies that succeeded, under the decree of dissolution, to the domestic tobacco manufacturing business formerly conducted by the combination. The companies are as follows: The American Tobacco Co., the Liggett & Myers Tobacco Co., the P. Lorillard Co., the R. J. Reynolds Tobacco Co., the American Snuff Co., the Weyman-Bruton Co., and the George W. Helme Co. Certain other companies were established by the decree which succeeded to other parts of the business of the combination not discussed in this report, namely, the foreign business, the domestic retail business, and the manufacture of accessory products.

The decree of dissolution allowed a *pro rata* distribution of the shares of the successor companies among the former shareholders of the combination and extended voting rights to the holders of the preferred stock. This extension of voting rights reduced the proportion of voting stock held by the principal holders thereof, namely, the 29 individual defendants in the dissolution suit, from about 56 per cent in the combination to about 35 per cent, on the average, in the successor companies.

The salient points brought out by this part of the report relative to the business of the successor companies, covering the two-year period following the dissolution of the combination (1912 and 1913), are as follows:

(13) That the several successor companies established in accordance with the plan of dissolution were much larger producers of tobacco products than any of the other companies.

(14) That a comparison of the successor companies' combined proportion of the total output of the country in the various branches of the tobacco business in 1913 with those of the combination in 1910 shows that the combined proportion of the successor companies was less in smoking and in fine cut; more in cigarettes and in snuff, and about the same in plug and little cigars.

(15) That in most branches there was a more equal distribution of business among the successor companies in 1912 and 1913 than there was directly after the dissolution.

(16) That, although there were no important changes in prices, the results for certain branches, particularly smoking and cigarettes, tend to show competition for business in 1912 and 1913 and an effort on the part of the several successor companies to fill in gaps in types of their business in which they were weak, though for certain other branches, particularly snuff, such competition has not been apparent.

(17) That in the snuff branch each of the three successor companies has practically a monopoly in its respective type and to a large extent a distinct sales territory; that the branch is characterized by unusually high profits and small advertising and selling costs.

(18) That the cost of leaf tobacco used by the successor companies in 1912 and 1913 in the plug, fine-cut, and cigarette branches was less, while in the smoking, snuff, and little-cigar branches it was more, than the cost of that used by the combination in 1909 and 1910.

(19) That the factory costs, other than leaf, of the successor companies in 1912 and 1913 and of the combination in 1909 and 1910 were not materially different.

(20) That almost invariably marked increases or decreases in

the volume of particular brands decidedly reduced or increased, respectively, factory costs other than leaf.

(21) That increases in selling cost after the dissolution were general, resulting from the duplication of selling organization and increased overhead expense, due to the division of the business.

(22) That there was a marked increase in the advertising expenditure of the successor companies as compared with that of the combination.

(23) That the aggregate amount of profit of the successor companies in 1913 was slightly less than that of the combination in 1910 in spite of a larger volume of sales.

(24) That the ratios of profit to net receipts less tax for the successor companies in 1913 were, in general, comparatively low in those branches or types in which competition for business was most pronounced, *e.g.*, plug-cut smoking and domestic and blended cigarettes, and very high in those in which competition was slight, *e.g.*, snuff.

(25) That on the book value of the total investment the earnings of the successor companies averaged 12.1 per cent in 1912 and 11.3 per cent in 1913, while the profit accruing to the holders of the common stock in respect to their interest was at a much higher rate.

(26) That on the total cost of investment, assuming that the cost of investment of the successor companies at the date of dissolution was the same as that of the combination in the corresponding branches of the business, the earnings of the successor companies averaged 14.6 in 1913. The earnings of the combination for the corresponding business in 1908 were 17.9 per cent and in 1910 about 17 per cent.

(27) That there have been no material changes in prices to the jobbers since the dissolution of the combination.

(28) That for all principal brands of the successor companies there have been practically no changes in prices to the consumer since the dissolution of the combination.

(29) That the high profits taken in conjunction with the practically unchanged wholesale and retail prices of tobacco indicate that there has been but little competition in price, but this is

explained in large part by the customary retail prices and other peculiar price-making conditions of the tobacco trade, including statutory provisions, which make it impracticable in most cases to increase the quantity sold at the customary price.

(30) That for the principal brands of plug tobacco, the manufacturer's cost in 1913 was approximately 50 per cent of the consumer's price, the internal-revenue tax 15 per cent, the manufacturer's profit 10 per cent, and the jobber's and retailer's margin 25 per cent; that for the principal smoking and cigarette brands the manufacturer's cost in 1913 was approximately 45 per cent of the consumer's price, the internal-revenue tax 20 per cent, the manufacturer's profits 10 per cent, and the jobber's and retailer's margin 25 per cent; and that for a number of the snuff brands the manufacturer's cost in 1913 was approximately 35 per cent of the consumer's price, the internal-revenue tax 15 per cent, the manufacturer's profit 20 per cent, and the jobber's and retailer's margin 30 per cent.

Other Companies

It was impracticable to obtain price, cost, and profit data from all companies, other than the combination and successor companies. However, data were secured from 64 of the other principal concerns manufacturing plug and smoking tobaccos, cigarettes, and cigars.

In respect to production, however, the total output of the country is available from the records of the Bureau of Internal Revenue, and these figures are used below in computing the percentages of the aggregate production of all other companies than the combination and successor companies.

In 1913 the plug output of the companies, other than the successor companies, covered by the investigation represented 65 per cent of the total production of all such other companies, the smoking output 78 per cent, and the cigarette output 50 per cent.

The salient points brought out by this part of the report relative to the business of companies other than the combination and successor companies, before and since the dissolution of the combination, are as follows:

(31) That for companies other than the combination and successor companies there were marked decreases in the proportions of their collective output in the plug, smoking, snuff, cigarette, and little-cigar branches, from 1905 to 1913.

(32) That compared with both the combination and successor companies the manufacturing costs of the other companies covered by the investigation were extremely high in practically all branches.

(33) That compared with either the combination or the successor companies the selling costs per unit of product of other companies investigated were extremely high in all branches.

(34) That the larger margins above manufacturing and selling costs of the combination and successor companies enabled them in most branches to spend from three to five times as much per unit of product for advertising or competitive purposes as the other companies investigated and at the same time to obtain practically the same or even greater rates of profit.

(35) That compared with the combination and successor companies the other companies investigated made an exceedingly poor showing of profits and that there was a marked decrease in profits of these companies in navy plug and Turkish cigarettes since the dissolution of the combination.

(36) That among companies investigated other than the Combination and successor companies the operations of the larger ones were, as a rule, the most profitable; and, in the manufactured tobacco business, those doing a general tobacco manufacturing business usually were more prosperous than those manufacturing exclusively one class of product. The operations of certain small companies, however, having especially popular brands were also profitable.

(37) That the companies other than the combination and successor companies which were the most successful in increasing their output were the ones that adopted the coupon advertising system, *i.e.*, the method of giving coupons, which are redeemable in either cash or articles of merchandise, as an inducement for trade.

(38) That the independent companies, like the combination,

did not generally reduce prices in 1901 and 1902, during which time the revenue tax was materially reduced.

(39) That the independent companies, like the combination, generally increased prices on smoking tobacco in 1910 to meet the increase in tax rate, and that the increase in price in most cases exceeded the increase in tax, but, like the combination, they did not increase prices on plug, cigarettes, or cigars.

IX

THE INTERNATIONAL HARVESTER COMPANY[1]

Conditions Leading up to Organization

THE International Harvester Co. was organized in August, 1902, under New Jersey laws, as a consolidation of the following companies:

McCormick Harvesting Machine Co.
Deering Harvester Co. (a partnership).
Warder, Bushnell & Glessner Co. (Champion).
Plano Manufacturing Co.
Milwaukee Harvester Co.

These concerns were the principal manufacturers of harvesting machines. In fact, the only other important manufacturers of such machines were a few companies located in New York State, engaged largely in trade with foreign markets, none of which did an extensive business in the principal domestic market for harvesting machines, namely, the grain-producing States of the Mississippi River basin.

The organization of the company followed a long period of keen competition among manufacturers of harvesting machines. An earlier attempt (in 1890) to bring about a general consolidation of the principal manufacturers of such machines proved abortive. Although a temporary organization was effected in that year under the name of the American Harvester Co., with $35,000,000 authorized capital stock, this had hardly been accomplished before the scheme fell through. From that time

[1] From Report U. S. Commissioner of Corporations, March 3, 1913, pp. 2-37. Omissions are not always shown in detail. *Cf.* also the Supreme Court opinion, Chapter XVIII, *infra*.

down to the organization of the International Harvester Co., the harvesting-machine industry appears to have been peculiarly free both from efforts at consolidation and also from the ordinary price agreements which were characteristic of many industries. In fact, the formation of the International Harvester Co. has repeatedly been attributed by some of its principal officers to the severity of competition during this period.

Cyrus H. McCormick, president of the company, in testimony in judicial proceedings in Missouri in 1908, described this competition as "fierce," and stated that a desire to remove what he termed "unbusinesslike methods" was one of the principal reasons for forming the consolidation. He further stated that during this period of competition a large portion of the sales of the competing companies were made below the listed prices.

Again, J. J. Glessner, formerly of the Warder, Bushnell & Glessner Co., makers of the Champion machines, referred to the competition as a "bitter fight," stating that his concern did everything that it possibly could to prevent its competitor from making a sale.

Still again, W. H. Jones, formerly of the Plano Manufacturing Co., stated explicitly that the merger was organized to abolish "fierce competition." This is shown by the following excerpt from his testimony in the Missouri proceedings:

> *Q.* So in order to get rid of this fierce competition you formed this new organization?—*A.* We had to do it or wind up the business. If we had not, we would have thrown all our men out of employment. The best thing to do was to get rid of the fierce competition, to get rid of the waste of money in canvassers. We have not half as many canvassers to-day as we did have.
>
> *Q.* The canvassers were necessary to maintain your competition?—*A.* Before that, we did it to beat one another out of business.
>
> *Q.* Is that not what you call competition?—*A.* Pretty sharp competition.
>
> *Q.* It was to get rid of that you made your combination?—*A.* Yes, sir; to better the entire thing; no question about that.

While it has also been claimed that economies of consolidation and the possibility of developing more satisfactorily the export trade were likewise considerations in bringing about the merger,

it may be accepted as established that the principal reason for the formation of the International Harvester Co. was the elimination of the competition complained of.

The severity of this competition has frequently been set forth as a full justification for the combination. It is important to point out, therefore, that notwithstanding this competition the profits in the business were large. Thus, the profits of the five combining concerns during the five years 1898–1902 aggregated nearly $43,000,000, or an average of nearly $8,600,000 a year. In the case of the McCormick concern, the profits for the year preceding the merger exceeded 12 per cent of the net assets as shown by its books, while those of the Deering business were nearly 18 per cent of such book assets, and those of the Milwaukee Harvester Co. over 11 per cent. Data for comparisons in the case of the other two companies are not available, but the profits of these apparently were smaller. These 1902 profits may have somewhat overstated the net earnings available for dividends, and the book assets are not an entirely satisfactory criterion for judging their exact significance, but it is certain that such profits were liberal. During this interval, moreover, there was a very great expansion in the volume of business of these companies. It is apparent, therefore, that while competition was severe it was by no means destructive.

It may be noted that many of the basic patents for harvesting machinery had expired, and were open to all who cared to engage in the manufacture of such machinery.

Methods by which the Company was Organized

Representatives of the company, and particularly of its financial organizers, have repeatedly insisted, at times in sworn testimony, that the combination was not brought about by the concerted action of the interests united, but instead that the five concerns were purchased independently the one of the other by the banking interests, and subsequently merged into a single organization.

These assertions may be sufficiently disposed of by citing from a statement made by Stanley McCormick and Cyrus

Bentley, legal counsel of the McCormicks, to G. W. Perkins on June 27, 1902, in New York City, and confirmed by a typewritten memorandum left with Mr. Perkins after having been revised at the head offices of the McCormick concern. This statement, which is given in full in this report, contained repeated references to conferences between representatives of the harvesting machine companies themselves, as the following excerpts show:

The McCormick and Deering people, in talking over how they might get together, estimated in the matter of good will that about two average years' profits ought to represent the good will of each company's business. In negotiations, not a great while ago, the Deerings rather expressed the opinion that if the McCormick and Deering companies were to come together it ought to be on a basis of about 53 for the McCormick company and 47 for the Deering, while the McCormicks' figures had been anywhere from 55 to 60 for the McCormick company and 40 to 45 for the Deering company. . . .

Mr. Glessner is president of this [the Champion] company. Mr. Harold McCormick saw him three or four weeks ago and sounded him as to what he would think of the several harvesting machine companies getting together. Mr. Glessner seemed to be very much interested in having it done, and said that his company would not be particular as to details or as to what influence would predominate. . . .

Mr. W. H. Jones is president of this [the Plano] company, and is the dominating influence. Mr. O. W. Jones, his brother, is vice-president. He visited Mr. McCormick about four weeks ago, and in a casual way asked if something could not be done in the way of combination. He remarked: "If you and I were appointed a committee of two to put this through, it wouldn't take us a week to wind it up" — giving the impression that he was anxious to see it put through. . . .

Mr. Deering has approached both the Plano and Champion companies, but so far as is known he has no option on either one. . . . The Deerings have indicated that they would prefer not to sell for cash, but would take securities and keep an interest in the management of the new organization.

Mr. Deering has urged that the whole trade be taken into the combination. Against this it has been suggested to him that if only 90 per cent were brought in, it would be quite possible to deal with another of the minor companies if any one made excessive demands.

That is, no minor company is probably essential to the combination, although the five named are undoubtedly the most desirable.

It is therefore conclusively established by documentary evidence that a consolidation of the five leading harvesting-machine makers had been considered, not merely by the bankers, but actively considered and discussed by the leading interests themselves, and this for a considerable period prior to the organization of the company. These discussions had specifically covered the relative values of some of the combining companies, the policy to be adopted with respect to other concerns than the five mentioned, and also the question as to who should have a controlling interest in the new organization. Moreover, the McCormick interests assisted the bankers in arranging for the acquisition of the Milwaukee Harvester Co.

Terms of Consolidation

The process by which the merger was actually accomplished involved a number of formal legal transactions. On July 28, 1902, four separate agreements were entered into between the McCormick, Deering, Plano, and Champion concerns, respectively, called the "vendors," and William C. Lane, called the "purchaser," all in substantially the same general form, but differing in certain details. These contracts set forth that the respective vendors were the owners of certain plants for the manufacture of harvesting machines, and that Lane, the purchaser, desired to acquire them for the purpose of selling them to a company to be formed subsequently, and referred to as the "purchasing company." In pursuance of these contracts and supplemental contracts of August 11, 1902, it was arranged that for the plants and other physical properties thus conveyed, together with the entire property of the Milwaukee Harvester Co., which was put in by the bankers as a going concern, and for the payment of the bankers' commission, $60,000,000 of stock was to be issued. An additional $60,000,000 of stock was to be issued for $60,000,000 cash. Of this amount $19,000,000 was to be contributed by the bankers and their associates, and $41,000,000 by the four vendor companies, as

follows: McCormick, $20,000,000; Deering, $16,000,000; Plano, $4,000,000; Champion, $1,000,000. By a subsequent arrangement, however, the McCormick and Deering interest agreed to contribute about $9,000,000 additional working capital, so that only about $10,000,000 was directly raised by the bankers. The payment of most of the working capital provided by the vendor companies was arranged through the assignment of bills receivable for collection.

The contracts further provided that the purchase price of the physical properties should equal their appraised value. Provision was made for valuing the good will on the basis of two years' profits, plus 10 per cent. These arrangements were subsequently modified by additional contracts.

Immediately after the contracts of August 11, 1902, were entered into, the International Harvester Co. was organized by a group of temporary or "dummy" incorporators, the certificate of incorporation being filed in New Jersey on August 12, 1902. Temporary directors were elected, who at once took under consideration a written offer from W. C. Lane to transfer the plants, good will, and other property, excluding receivables, of the McCormick, Deering, Plano, and Champion concerns, together with the Milwaukee company as a whole, and working capital of $60,000,000. The plants, good will, etc., were nominally valued at $132,000,000, thus making a total nominal value of $192,000,000. In payment therefore Mr. Lane offered to accept the entire capital stock of the International Harvester Co., namely, $120,000,000 par value, subject to a provision that if any additional stock were issued by the company prior to July 1, 1903, on account of the nominal surplus of $72,000,000, then this original $120,000,000 of common stock should become preferred stock and the additional stock should be common stock, to be issued to the holders of the preferred, *pro rata*.

On August 13, 1902, W. C. Lane and E. H. Gary (chairman of the United States Steel Corporation) appeared before the temporary board of directors and explained Lane's offer, which was promptly accepted. Resolutions were adopted to the effect that the properties and working capital were worth the amount stated by Lane ($192,000,000), and that the treasurer should

enter the proper amounts in the books of account, including a surplus of $72,000,000.

This surplus of $72,000,000 was entirely arbitrary, and, in fact, wholly fictitious. It is obvious that at the time it had not been definitely decided whether the company should be organized with a capitalization approximately commensurate with the value of its assets or whether it should issue stock greatly in excess of that capitalization.

On the same day (August 13) the new stockholders took control of the company. The temporary directors resigned, and 18 directors were elected in their places. Of these 18 directors, 10 were largely interested in the four companies merged; 3 others had been connected with such concerns or individuals as counsel; 4 represented either the bankers (J. P. Morgan & Co.), or capitalists associated with them; the only remaining director was put in to comply with the corporation laws of New Jersey requiring a resident director.

On the same day also the temporary officers of the company resigned and the principal officers elected in their places were as follows: Cyrus H. McCormick, president; James Deering, Harold F. McCormick, W. H. Jones, and J. J. Glessner, vice presidents; Richard F. Howe, secretary and treasurer. The executive committee, of which Charles Deering was made chairman, included the principal representatives of four of the companies merged, and G. W. Perkins, who was also made chairman of the finance committee.

An important step in carrying out the original contracts of July 28, 1902, with the principal companies entering the merger, namely, the establishment of a voting trust, was made on August 13 by execution of the voting trust agreement and the appointment of the following persons as voting trustees, namely, George W. Perkins, Charles Deering, and Cyrus H. McCormick.

The actual consummation of the merger, as explained in more detail in the full text of the report, involved certain additional contracts. This was due to the fact that since the contracts of August 11, 1902, limited the total issue of capital stock to $120,000,000, and since $60,000,000 of this was to be issued for working capital, there would have been nothing left for the bankers and promoters or for the purchase of the Milwaukee

Harvester Co. in case the appraisal of the physical properties of the four vendor companies amounted to as much as $60,000,000. The contemplated compensation of the bankers was $3,000,000 in stock, and the cost of the Milwaukee company (put in by the bankers), together with certain expenses, amounted to more than $3,500,000. If these items were to be provided for, therefore, there would be only about $53,000,000 of stock left to pay for the plants and other physical properties of the four vendor companies. It was agreed, therefore, by an additional contract dated August 17, 1903, that certain specified amounts of stock should be allotted to each of the vendor companies in lieu of the amounts to be determined by the appraisals. The amounts agreed upon, subject to slight adjustments, were as follows:

McCormick company	$26,321,656.86
Deering company	21,362,554.64
Champion company	3,372,185.91
Plano company	2,193,603.09
Total	$53,250,000.50

It will be seen, therefore, that the elaborate appraisals made of the physical properties of the vendor companies really did not determine the amounts of stock issued. Subsequently, however, these appraisals, when completed, were used to some extent for bookkeeping purposes. The final allotment of the $120,000,000 capital stock of the International Harvester Co. is briefly summarized in the table on the following page.

The table is in the main explained by the preceding discussion. It will be noticed that certain small amounts were deducted from the "plant stock" issued to the bankers and to the McCormick and Deering interests, together aggregating $150,000, this amount being divided equally between the Champion and Plano interests. Again, while $3,000,000 of stock was allotted for the acquisition of the Milwaukee Harvester Co., on actual appraisal the value was established at $3,148,196.66. The excess was issued to the bankers out of the cash stock. The banking interests also raised $10,000,000 of cash capital (including $60,000 paid in by the temporary incorporators). The remaining cash capital was raised by the various manufacturing interests as indicated in the table (on the next page).

DISPOSITION OF ORIGINAL $120,000,000 CAPITAL STOCK OF INTERNATIONAL HARVESTER CO.

PLANT STOCK

J. P. Morgan & Co.:			
Commission	$3,000,000.00		
Less contribution to Champion and Plano companies	42,857.14		
	2,957,142.86		
Milwaukee Harvester Co.	3,000,000.00		
		$5,957,142.86	
McCormick interests:			
Original allotment	26,321,656.86		
Less contribution to Champion and Plano companies	59,142.86		
		26,262,514.00	
Deering interests:			
Original allotment	21,362,554.64		
Less contribution to Champion and Plano companies	48,000.00		
		21,314,554.64	
Plano interests:			
Original allotment	2,193,603.09		
Plus contributions from other interests	75,000.00		
		2,268,603.09	
Champion interests:			
Original allotment	3,372,185.91		
Plus contributions from other interests	75,000.00		
		3,447,185.91	
Organization expenses (excluding Milwaukee company and incorporators' stock):			
Sold	611,803.34		
On hand	138,196.16		
		749,999.50	
			$60,000,000.00

CASH STOCK

J. P. Morgan & Co.:			
Cash	$9,940,000.00		
Incorporators	60,000.00		
Milwaukee excess	148,196.66		
		$10,148,196.66	
McCormick interests:			
Original subscription	20,000,000.00		
Subsequent subscription	4,886,190.13		
		24,886,190.13	
Deering interests:			
Original subscription	16,000,000.00		
Subsequent subscription	3,965,613.21		
		19,965,613.21	
Plano interests		4,000,000.00	
Champion interests		1,000,000.00	
			$60,000,000.00

Of the $120,000,000 capital stock of the company, $103,144,660.98, or 86 per cent, was received by the McCormick, Deering, Champion, and Plano interests. The McCormick interests alone received $51,148,704.13, or 42.6 per cent, and the Deering interests $41,280,167.85, or 34.4 per cent. These two groups together, therefore, received no less than 77 per cent of the total capital stock. As a matter of fact, while the voting trust technically gave the McCormick, Deering, and Morgan interests equal voice in the management of the company, the predominating influence appears to have been with the McCormick interests.

Position of the International Harvester Co. at its Organization

At its organization the International Harvester Co. controlled approximately 85 per cent of the total production of harvesting machines in the United States. While exact data on production are not available, statistics of sales show that in binders the companies composing the new combination had handled approximately 90 per cent of the business in the year prior to the merger; in mowers, about 81 per cent; and in rakes, about 67 per cent. This is shown by the following comparison of sales in the 1902 season:

	Sold by International Harvester Co. Companies, Season of 1902[1]		Sold by Independent Companies, Season of 1902[2]	
	Number	*Per cent*	*Number*	*Per cent*
Binders	180,024	90.9	18,128	9.1
Mowers	297,880	81.2	68,890	18.8
Rakes	165,219	67.0	[3] 81,376	33.0

The important machines were binders and mowers, and combining these it may be safely said that 85 per cent of the

[1] Number produced in case of the Milwaukee company.
[2] Number produced in case of the Osborne company.
[3] Number for independents partly estimated.

business was handled by the new consolidation at its organization.

The McCormick company had much the largest production for each class of harvesting machines; the Deering company was second in each case. The Champion concern stood third with respect to binders and mowers, while the Milwaukee had the smallest output for all the principal machines.

Comparison of Capitalization with Investment

As already shown, of the capital stock of $120,000,000 at the time of organization, $60,000,000 was issued for plants, inventories, and similar property, and $60,000,000 for working capital. The appraised value of the property acquired by the $60,000,000 of "plant stock," so called, was $67,000,000 exclusive of good will, and the company claims therefore that it started with a surplus of $7,000,000. This surplus was later written off. As a matter of fact, this appraisal of $67,000,000 for the property acquired by the plant stock was in excess of a fair valuation, exclusive of good will. As shown below, the Bureau has arrived at a valuation for this property of only about $49,100,000. The difference between this and the $60,000,000 of stock issued therefor, so far as covered by any value whatever, must be set against good will.

The net result of the Bureau's readjustment of the valuations was to give a total of $49,117,356.08 as the maximum valuation of the physical property and inventories acquired by the International Harvester Co. from the five companies forming the combination, as shown in the table on the opposite page.

The Bureau believes that while this valuation might be somewhat reduced if all the facts were available, any adjustment which would be made would not be of decisive importance. This maximum valuation of $49,100,000 compares with $60,000,000 "Plant stock" issued for such property and for promoters' expenses and services. This, as already noted, leaves a difference of, roughly, $10,900,000 to be represented by intangible considerations, such as good will.

FIVE PREDECESSOR COMPANIES: VALUATIONS OF PHYSICAL PROPERTIES, 1902

[N. B. — No book values available for Champion and Plano, therefore total book valuations cannot be given.]

	Harvester Co.	Bureau	Difference
Factory real estate, buildings, and machinery	$23,270,218.14	$20,787,435.09	$2,482,783.05
Agency property	2,249,882.33	2,173,539.56	76,342.77
Railroads	2,579,324.82	510,645.22	2,068,679.60
Ore, coal, iron, and steel	9,574,138.79	1,858,326.92	7,715,811.87
Timber	1,874,800.22	839,552.98	1,035,247.24
Miscellaneous [1]	1,979,702.93	1,717,206.00	262,496.93
Inventories	25,548,162.42	21,230,650.31	4,317,512.11
Total	67,076,229.65	49,117,356.08	17,958,873.57

Good Will

The Bureau has not attempted to value any good will which the constituent concerns of the consolidation may have brought into the merger. In the original contracts on which the combination was based it was agreed that good will should be valued at the sum of the profits of the two preceding years plus an additional 10 per cent. By this method of valuing good will, which was more or less commonly used among manufacturers, the total value of the good will was placed at about $20,800,000. If good will be allowed for the Milwaukee company on the same basis, the total good will of the combination would be about $21,300,000.

Without indorsing this valuation, the Bureau is nevertheless of the opinion that there was a substantial good-will value brought into the merger. The McCormick, Deering, and Milwaukee companies, as already shown, made a liberal rate of profit while operating independently. This fact, together with the fact that their business had been long established, and that their machines were always sold under brand name, indicates

[1] For Milwaukee company includes net working capital after deducting $148,196.66 for plant stock excess.

that these concerns must have had a large good will. Against this there should be set the fact that the harvesting-machine business had apparently been somewhat overdone prior to the merger, and that there was some danger of a loss of good will as the very result of the formation of a combination or trust like the International Harvester Co.

Working Capital

The stock issued for working capital, so far as the vendor companies are concerned, was paid in chiefly through the collection of bills receivable of the principal constituent companies. About $10,000,000 of this cash stock was subscribed for at par by the bankers. The Bureau made an extended investigation of the accounts relating to this provision of working capital, and so far as these may be relied upon they indicate that the full amount of $60,000,000 was actually paid in in cash. Representatives of the International Harvester Co., moreover, repeatedly declared that there was no deduction or allowance from this cash payment, but that the full amount was actually paid in as represented.

Subsequent Acquisitions and Extensions

Immediately after its organization and almost continuously thereafter the International Harvester Co. pursued the policy of expanding its control over the farm-machinery business, not only in harvesting machines but also in various other branches. This process may be divided into three parts: (1) Acquisition of competitors in the harvesting-machine business; (2) acquisition of concerns making other lines of farm machinery; and (3) construction of new plants in the United States and in various foreign countries for the manufacture of harvesting machines and other farm machinery.

Shortly after its organization, namely, in January, 1903, it acquired secret control of D. M. Osborne & Co., of Auburn, N. Y., the most important manufacturer of harvesting machines not originally taken into the combination. This secret control was maintained for nearly two years. During this period the Osborne company was operated and advertised as an independent

concern, and these representations were supported by its managers in sworn statements that it was an independent company. The International Harvester Co. claims that this was done to enable the original owners to collect certain obligations due them and that it was done at their request. While the Osborne company had a valuable line of tillage implements, its chief importance lay in the production of harvesting machines, in which it had an extensive foreign trade. In selling this concern the two largest active stockholders of the Osborne company (T. M. Osborne and Edwin D. Metcalf) covenanted with the International Harvester Co. that they would refrain from engaging independently in the same business for a period of ten years.

In a similar secret way the International Harvester Co., between 1903 and 1904, acquired control of several other concerns which competed in the manufacture of harvesting machines and twine, . . . and operated them without disclosing such control for various periods. In the case of the Minnie Harvester Co. it is claimed that this method was used merely to facilitate the liquidation of the company.

Negotiations were also had with a number of other competing makers of harvesting machines with a view to acquiring their properties or business, in whole or in part. . . . These negotiations, however, were not consummated.

Extensions Into New Lines

Aside from these acquisitions of competing concerns, the International Harvester Co. has greatly expanded its business by branching out into new lines of manufacture or sale. Among the most important lines which the company entered in this way were manure spreaders, wagons, plows, and seeders. Here again expansion was accomplished in part by the acquisition of concerns already organized.

By thus extending its business into a number of new lines the International Harvester Co. not only increased the extent of its business, but where it was thus provided with satisfactory goods, it was able to accomplish their sale more successfully than some of the former owners, partly on account of its larger financial

resources and elaborate selling organization, and also in part on account of the pressure it was able to exert to induce dealers to handle these new lines. To a considerable extent such dealers were not allowed to handle its harvesting machines (in which it had obtained, as already shown, a substantially monopolistic position by means of combination), unless they would take these new lines also. It is apparent, therefore, that not only did the company's strong position in the harvesting-machine business facilitate its entrance into new lines, but also that these new lines in turn afforded a further means of maintaining its position in the harvesting-machine business itself.

Construction of New Plants

The International Harvester Co. extended its business in the manufacture of harvesting machines, and also in the production of new lines by building new plants, both in the United States and in foreign countries. Some of the old harvesting-machine plants were remodeled and used for making new lines of farm machinery. The most important new plant built in the United States was a large tractor plant at Chicago. The company, furthermore, greatly enlarged its plants for the manufacture of iron and steel.

The most important new construction of the company was in foreign countries, where large factories have been built for the manufacture of harvesting machines and other farm machinery, namely, in Canada, Sweden, France, Germany, and Russia.

Organization of the International Harvester Co. of America

One important feature of the policy of the combination was the use of the Milwaukee Harvester Co., as a selling agency for the International Harvester Co. of New Jersey. For this purpose the name of the Milwaukee company was changed in September, 1902, to International Harvester Co. of America; the capital stock, fixed at $1,000,000, is all held by the New Jersey company. The officers and directors of the American company were until 1910 all officers or directors of the International Harvester Co. of New Jersey. Apparently, a separate

organization was adopted in order to avoid heavy taxation and the delay and difficulty of procuring new licenses to do business required in various States. Such licenses were often prohibited in case the foreign corporation applying was a trust or combination in restraint of trade.

Rearrangement of Capitalization

In 1907 the International Harvester Co. divided its capital stock of $120,000,000 into $60,000,000 of preferred and $60,000,000 of common stock. Furthermore, in 1910 a stock dividend of $20,000,000 of common stock was declared from surplus, making the capital stock of the company $140,000,000, consisting of $60,000,000 preferred and $80,000,000 common. In this connection it should be noted that the voting trust was finally dissolved in August, 1912, and the stock distributed among the holders of the stock trust certificates. The great bulk of the stock of the company has throughout been closely held by a comparatively few interests, who have also been active in the management of the concern. It will be recalled that the McCormack interests had approximately 43 per cent of the stock at organization and the Deerings about 34 per cent.

On January 29, 1913, the directors of the International Harvester Co. announced that they had transferred to a new concern, the International Harvester Corporation, all of the foreign plants and all of the foreign business, also certain domestic plants engaged in the manufacture of the so-called new lines, together with certain assets pertaining thereto. This company is capitalized at $70,000,000, consisting of $30,000,000 of 7 per cent preferred stock and $40,000,000 of common stock. The present International Harvester Co., the name of which it is proposed shall be changed to International Harvester Company of New Jersey, will retain the remaining assets, and its capital stock will be reduced to $70,000,000, likewise consisting of $30,000,000 of 7 per cent preferred and $40,000,000 of common. For the $70,000,000 stock of the present company canceled, the stockholders will be entitled to receive cash or a *pro rata* distribution of the stock of the new International Harvester Corporation.

This action by the company is admittedly taken in view of the pending dissolution suit of the United States Government against the company. This rearrangement of capitalization was approved by the stockholders on February 10, 1913. If intended as part of a plan of disintegration the Bureau regards this method of division as very unsatisfactory.

Present Position of the International Harvester Co.

The original monopolistic position of the International Harvester Co. in harvesting-machine lines had been substantially maintained up to the close of 1911, as the following table shows:

PROPORTION OF THE HARVESTING-MACHINE BUSINESS OF THE UNITED STATES CONTROLLED BY THE INTERNATIONAL HARVESTER CO. IN 1911[1]

Machines	Manufactured in United States	Sold in United States
	Per cent	*Per cent*
Grain binders	87.0	87.2
Mowers	76.6	74.6
Rakes	72.0	68.0

For the new lines of farm machinery it is not possible in most cases to show the precise position of the International Harvester Co., but in several of them it has acquired a very considerable proportion of the trade. For spreaders the Bureau has obtained statistics covering a large majority of the independent production and sale in the United States, and has made estimates for the remainder which it is satisfied are approximately correct. A comparison of these figures with those of the International Harvester Co. shows that the company has about 55 per cent of the 1911 production in the United States and about 50 per cent of the sales. A comparison for disk harrows on a similar basis, for which the Bureau also had returns

[1] Percentages based on practically complete returns for binders and mowers, but partly on estimates for rakes for which the returns covered about 93 per cent of the total business.

for a substantial majority of the total independent business, indicates that the Harvester Co.'s proportion of the number produced was at least 43 per cent, and its proportion of the number sold at least 37 per cent.

For certain other lines also the International Harvester Co. has acquired a large proportion of the business, but satisfactory data are not available to show its percentage. In the case of wagons, the International Harvester Co. had nothing at the start, but according to the best estimates that can be made by the Bureau, had in 1911 about 15 per cent of the number manufactured in the United States and about 13 per cent of the number sold, although the total production of farm wagons in the United States has decreased in recent years.

It is apparent, therefore, that the International Harvester Co. not only has maintained a high degree of monopoly in the harvesting-machine business proper, but has also become an important factor in several new lines.

The expansion of these various concerns is one of the most significant features of the farm-machinery industry to-day, and one involving possibilities of great importance. It is important to note that these new developments have been made on the principle of carrying a so-called full line of farm machinery, although it should be understood that no company, not even the International Harvester Co., has a really complete line.

Profits of the International Harvester Co.

The chief feature of the profits of the International Harvester Co. is the increase from a low rate in the early years of the organization to a rather high rate in recent years, averaging about 12½ per cent on the net assets, as computed by the Bureau, for the period 1909–1911; figures for the year 1912 are not available.

The net assets and profits of the company and the rate of profit on the net assets for 1903–1911, as thus computed by the Bureau in both cases, are shown in the following table. The rates are computed on the net assets at the beginning of each year; this is the method adopted by the company in computing the rates on capital and surplus.

RATE OF NET EARNINGS OF THE INTERNATIONAL HARVESTER CO. ON NET ASSETS, EXCLUSIVE OF GOOD WILL, AS COMPUTED BY THE BUREAU, BY YEARS, 1903–1911

Year Ending Dec. 31 –	Net Assets, Exclusive of Good Will	Net Earnings	Profit on Assets at Beginning of Year	Year Ending Dec. 31 –	Net Assets, Exclusive of Good Will	Net Earnings	Profit on Assets at Beginning of Year
			Per cent				*Per cent*
1902[1]	$109,117,356.08	—	—	1908	$122,522,298.85	$10,179,726.02	8.73
1903	106,314,179.00	$796,822.92	[2]0.73	1909	134,781,142,61	16,458,843.76	13.43
1904	107,196,624.97	5,682,445.97	5.34	1910	144,589,739,95	17,208,597.34	12.77
1905	109,907,909.12	7,511,284.15	7.01	1911	—	16,638,703.28	11.51
1906	112,514,855.99	7,406,946.87	6.74	Total	1,063,486,679.40	90,111,087.15	8.47
1907	116,542,572.83	8,227,716.84	7.31				

Hence, while the profits of the International Harvester Co. on the average for the whole period of its operations have not been excessive, the profits for the three-year period, 1909 to 1911, inclusive, have been distinctly high. In judging of the reasonableness of this rate of profit it is proper to consider the fact that the risk of the company's business is comparatively small, owing to its world-wide character, which to a large degree is an insurance against the effects of local disturbances of business prosperity. It is also important to bear in mind the fact that the business rests in part on a monopolistic basis, which not only tends to reduce the element of risk, but also makes it desirable from a public standpoint that the rate of profit should not be higher than a reasonable return to the capital invested.

In the course of operations a large part of the net earnings of the company were left in the business and not distributed in dividends, so that by the end of 1908 all original deficiency in physical assets, compared with capital stock, according to the

[1] Oct. 1.

[2] This covers 15 months, but no change has been made for this period nor for the average of all the years on that account. This is in harmony with the company's method of treatment. For an explanation of the exceptionally low earnings of 1903, see text.

Bureau's computations, had been wiped out and a surplus balance established of $2,522,298.85. In 1910 the capital stock was increased, as already stated, to $140,000,000, and at the end of 1911 a surplus existed, according to the Bureau's computations, of $13,028,443.23, exclusive of good will. This surplus may be compared with the surplus shown by the balance sheet of the company for December 31, 1911, of $23,390,946.90, which is also exclusive of good will.

The difference is the net result of the Bureau's reduction of the assets on the one hand and its reduction of the reserves on the other. The Bureau has added nothing for subsequent appreciation which doubtless would be necessary if a fair appraisal were made at the present time.

Profits in Particular Lines and in Export Trade

A noteworthy feature of the business of the company is that the rate of profit, whether on sales or on investment, for the highly monopolistic lines — that is, grain and grass harvesting machines — is very much higher than the corresponding rates for several of the important new lines, such as wagons and spreaders, where the company encounters a greater degree of competition, and the same is true of twine. Thus, the rate of return on wagons, in which the company's percentage of the business done is as yet relatively low, is admittedly much less than in the monopolistic lines; and even in manure spreaders, where the company does approximately one half the business in the United States, the profits are comparatively low, probably due to the agressive sales policy adopted by the company.

Comparing the foreign business of the International Harvester Co. with the domestic business, there are comparatively few exceptions, apparently, to the statement that the prices to the retail dealer or to the farmer are higher abroad than in the domestic market. This is due largely to the fact that the business in foreign markets must bear a large expense for freight and generally for duty, while the selling expenses likewise are often high. The only proper basis of comparison for the returns to the company is found in the net price received at the factory

in the United States, due account also being taken of the extra cost of packing or other extra costs of machines made for export. The company maintains that its net returns on this basis are higher for the export than for the domestic trade, but its own accounts show that this is by no means universally the case.

Productive Efficiency and Financial Resources

Cost of Production. — The International Harvester Co., generally speaking, has an advantage over independent manufacturers with respect to the cost of production of its machines. This is especially marked in the case of grain binders, the most important of the harvesting machines. Thus the average factory cost of binders for the International Harvester Co. at its domestic plants for the two years, 1910 and 1911 combined, was $56.32, and ranged from $54.11 to $73.78 at the different plants. While the company produces most of the iron and steel required — on which its subsidiary steel company makes a very large profit — the cost of these materials to its implement plants is based on prevailing market prices, so that its costs in this respect are comparable with those of the independent producers. For the four independent companies that reported to the Bureau the cost of their binders, the average factory cost for the same period as computed from the data reported by them was $70.83.

These figures of factory costs do not take account of general and miscellaneous expenses, which are not ordinarily reckoned in the costs of machines at the factories, nor for a much heavier selling expense which for binders sometimes amounts to $20 or even $25 per machine. If these expenditures are prorated over the cost of production, both for the International Harvester Co. and the independents, the average cost of binders for the International Harvester Co. becomes $58.57, and for the four independents $76.18.

A proper understanding of these relations of cost of production to the competitive position of the independent binder manufacturers requires consideration also of the question of selling expense. The selling expense per binder for the International Harvester Co. is considerably higher than the average selling

expense of the independents, and this fact partly compensates the latter for their higher average costs of production. Nevertheless the margin of profit between prices and cost of production and selling expense combined is markedly lower for the independents than for the International Harvester Co. Apparently the high selling expense of the International Harvest Co. is due to the policy of maintaining a very elaborate selling organization, which gives it a strong hold on the trade and helps to secure to it a large volume of business. Apparently it is the company's policy thus to maintain an expensive selling organization to push the sale of its goods rather than reduce prices on some of its most important lines, particularly harvesting machines.

Similarly in the case of mowers and rakes, for which the Bureau had sufficient data for comparing the costs of the International Harvester Co. with those of independents, it was found that the average cost of manufacture at the plant of the International Harvester Co. for the years 1910 and 1911 combined was lower than the average cost of the independents reporting.

The foregoing comparisons of production costs indicate one of the most important advantages enjoyed by the International Harvester Co. The striking advantage it has with respect to cost of production of binders, taken in connection with the great importance of this machine in the farm-implement trade, is one of its chief elements of power.

Financial Resources. — Another chief element of strength of the International Harvester Co. is the possession through combination of large financial resources. This is reflected principally in three ways: First, the ability to reap the advantages of large-scale production already described; second, the ability to carry a full line and maintain an elaborate selling organization; third, the ability to grant long terms of credit.

Most of the concerns which compete with the International Harvester Co. are not full-line concerns. Those which make harvesting machines in most cases do not produce other lines to an important extent. Again, most of those which make other kinds of farm machines have only a few lines, and sometimes only one. On the other hand, there are three large full-line companies, the operations of which, in this connection, are compared with the International Harvester Co.

Except possibly for the three full-line companies mentioned above, the International Harvester Co. enjoyed a great advantage with respect to the distribution of similar kinds of implements, in so far as the methods of distribution employed were similar. There are generally great differences in the selling expense of different kinds of machines, owing to different methods and customs regarding sale and distribution, these being partly due to the technical requirements of the business. Custom has generally established a more elaborate system of distribution for harvesting machines than for tillage implements, while the character of the goods themselves and the necessity for "setting up," etc., in the case of harvesting machines involves a greater expense than for most other lines. While nearly all companies engaged in the distribution of certain harvesting machines utilize an elaborate organization for distribution, full-line companies with great financial resources are, to a considerable extent, able to apply the same system to other lines, such as manure spreaders, engines, and wagons. While this undoubtedly increases their actual outlay for selling expense per unit in these lines, in so far as they eliminate the jobber, they obtain thereby a higher price, generally, for the goods. Moreover, they are thereby enabled to obtain a much stronger hold on the trade; for example, by selling directly to the local dealer instead of to the jobber, and, furthermore, by getting in direct contact with the farmer, through the employment of canvassers and other salesmen.

The granting of long terms of credit was originally developed in the harvesting-machine industry on account of the general inability of farmers to purchase expensive machines, like binders, for cash, but it has been continued, to a certain extent at least, as a special means of getting trade by those concerns which had ample financial resources. Moreover, it has been extended by them to other lines of farm implements of a less expensive character, in which this custom was not developed until a comparatively recent time.

The International Harvester Co., which, through combination, acquired extraordinary financial resources, not only perpetuated the system of selling harvesting machines on long terms of

credit, but, more conspicuously than any other concern, has extended this system to its new lines. This system of selling these new lines on long terms of credit has made it difficult for the manufacturers of such lines, except possibly other full-line concerns, to meet its competition, and is the principal complaint which they make regarding the present conditions of business. Representatives of the International Harvester Co. claim that its leading competitors grant equally long credits and declare that its policy is to develop as far and as rapidly as possible the system of cash sales, that is, cash payment in the same season as the goods are purchased, and that discounts for cash are allowed for this reason. While in some localities there has been a great increase in the proportion of cash sales, nevertheless, taking the business of the International Harvester Co. as a whole, it appears that the proportion of sales on long credit (*i.e.*, one or more years) to total sales was higher in 1911 than at the beginning of business. This increase in the proportion of credit sales is partly due, at least, to the application of long credits to the new lines of goods for which they were formerly uncommon.

The International Harvester Co. is enabled to pursue this policy, as already stated, because of the large resources it acquired through combination, and furthermore, it has been aided therein by financial support of an exceptional character through its connection with J. P. Morgan & Co., its fiscal agents. The company has also secured large loans from John D. Rockefeller, father-in-law of one of the McCormicks.

Competitive Methods of International Harvester Co.

While, as just shown, the main source of the International Harvester Co.'s power was the consolidation of competing manufacturers and the accompanying increase in financial resources, the company's position in the industry has been maintained to some extent by objectionable competitive methods.

In discussing the competitive methods of the company it should be recognized that some practices which might be regarded with indifference if there were a number of competitors

of substantially equal size and power, may become objectionable when one competitor far outranks not only its nearest rival, but practically all rivals combined, as is true of the International Harvester Co. so far as several of its most important lines are concerned.

It should also be observed that during the first two years of its operations the company was badly organized, and that instead of a harmonious policy, "divisions" corresponding to the five old concerns acquired were maintained, and that under this arrangement various objectionable practices prevailed, some of which appear to have been subsequently abandoned. At the same time there has continued to be a rather general complaint among dealers, and competing manufactures as well, against the methods employed by the company.

Among such objectionable competitive methods here discussed are:

(1) Maintenance of bogus independent companies in the early years of the company's operation.

(2) Attempts to force dealers carrying its harvesting machines into carrying additional lines or certain International lines exclusively. At an earlier date the contracts of the Harvester company contained an exclusive clause for harvesting machines.

(3) Efforts to secure an undue proportion of desirable dealers in a given town by giving only one of its several brands of harvesting machines to a dealer, thus tending to restrict the outlet for competitive goods.

(4) Use of "suggested price" lists, tending to influence the final retail price; earlier the contracts themselves provided for fixing of retail prices by the company.

(5) Occasional discrimination in prices and terms.

(6) Misrepresentations by salesmen regarding competitors.

Pretended Competition in Early Years

So far as the maintenance of bogus independent companies is concerned, this has already been referred to in discussing the acquisitions of the Osborne, Minnie, Aultman-Miller and Keystone concerns. The impropriety of continuing the operation

of these companies under the old names, without disclosing the real ownership, after they had been acquired by the International Harvester Co., is obvious. Some of these concerns were openly advertised as independent. It should be repeated that in some cases it is alleged that the ownership was concealed merely to facilitate the liquidation of the old concern, but the Bureau does not regard this as a justification of the practice.

Coercion of Dealers to handle International Harvester Co. Goods

Exclusive Contract. — In 1905 and previous years the Harvester company's usual commission-agency contract contained substantially the following clause:

> Said agent especially agrees not to accept the agency for or to be interested in the sale of any grain binder, header, corn binder, husker and shredder, reaper, mower, stacker, sweep rake, hayrake or hay tedder, other than those manfactured by the International Harvester Company, either directly or indirectly, nor to permit any one acting for him as employee, agent, or partner, so to do while acting as agent for the said company under this contract, and said agent agrees to pay said company on demand as liquidated damages, twenty-five dollars for each grain binder, header, or corn binder; fifty dollars for each husker and shredder; ten dollars for each mower, reaper, or stacker; five dollars for each sweep rake, hayrake, or hay tedder sold in violation of this paragraph of this contract.

It is obvious that the use of this clause in the contract, even if not enforced, would have a powerful effect upon most dealers.

It is indicative of the real intent of this clause that it was eliminated from the contract after 1905, when antitrust proceedings against the company were threatened in several States. In fact, in Texas the use of this clause was discontinued as early as October, 1902. On the other hand, it should be noted that this clause was customary among harvesting-machine companies prior to the merger and has been used by some other companies in the implement trade even since it was abandoned by the International Harvester Co. It is much more objectionable, however, when used by a concern which has a monopolistic position.

Exclusive Handling. — After the elimination of the exclusive

clause from dealers' contracts, other means were not infrequently employed to secure the same end. In a considerable number of instances reported to the Bureau, salesmen of the International Harvester Co. endeavored to prevent the handling of a competitor's line by threats to discontinue the dealer's agency for the International Harvester Co.'s machines, and in some instances canceled or discontinued the dealer's agency when he insisted upon handling an independent line. The company asserts, however, that such practices are contrary to its policy.

"*Full-line*" *Forcing.* — This complaint was a rather general one among the dealers interviewed. Obviously it is difficult to say just where this practice of trying to force dealers to take additional kinds of products ceases to be legitimate competition and becomes objectionable. The International Harvester Co., like any other concern, desires to push the sale of its goods, and naturally is disposed to take advantage of the fact that it has certain desirable machines, in order to force the sale of its newer lines. Aside from any question as to motive, it is apparent that any concern having a monopoly of such an article as harvesting machinery has an enormous advantage in forcing its entrance into new fields, and that this advantage is very susceptible of abuse. There were numerous complaints that the salesmen of the company attempted to force dealers to take on lines in addition to those already handled, frequently under penalty of loss of their agencies for the company's harvesting machines. Frequently, however, it appeared that these threats were not carried out.

Effort to secure Undue Proportion of Dealers

As a rule there are not more than three dealers in farm machinery in an ordinary town in the grain States. It is the policy of the International Harvester Co., in general, to allow a given dealer to handle only one of its several brands of harvesting machines, thus absorbing the services of a large number of these dealers; of course, not all of the company's brands are handled in every town. Complaint is made that this tends to give it such an undue proportion of dealers as to restrict the outlet for competitors' goods. The company, however, expressly denies

that in adopting this policy of distributing its brands it is actuated by any desire to handicap its competitors in this way. The company's position on this point is illustrated by the following excerpt from testimony of the assistant general manager to the Bureau:

Q. I understand then that your position is that the company does not place its brands in this way for the purpose of handicapping its competitors; and you also contend that, regardless of intent, the practical effect is not to handicap your competitors?—*A.* It does not. Its sole purpose is to get more active representation of your goods, which you cannot do if you allow them to get into the hands of one man in a town. He will not give your customers the same consideration, the same service, as he will if he is handling a less number. Not only do we not try to eliminate them in that way, but it is a matter of real benefit to us in new sections when a competitor will get a real live, active man in the trade. We sell more goods than we could do if we gave all our lines to one man and there was not any competitor there.

However, it seems significant that the record in the Government suit shows that in 1903 a report of the sales committee of the International Harvester Co. of America, which was approved by the executive committee, contained the following statement:

We believe that so long as there is competition it is desirable for the International Harvester Co. to maintain five selling organizations for the purpose of getting the largest amount of effort from the greatest number of local agents without expense to the company, and for the purpose of utilizing in its own business as much as possible of the available local agency material rather than permit any of it to become available for competitors.

Still again, in 1902, when the exclusive contract was discontinued in Texas, the executive committee of the International Harvester Co. of America directed each division of the company "to discourage any agent in Texas from handling more than one brand of machine."

These official statements seem to show conclusively that the distribution of brands among various dealers in the manner indicated was at one time the result of a settled policy of the company to secure as many of these dealers as it could for its

own business, and with a view to embarrassing competitors. In view of these official statements, the fact that the company still distributes its brands in this way seems significant. Practically, the supply of dealers even in the smaller towns usually has been sufficient to prevent anything like an effective monopoly of these channels of distribution, although it does appear that the company's practice in this respect has to some extent handicapped its competitors.

Issue of "Suggested-price" Lists

Formerly the commission agency contracts of the International Harvester Co. expressly provided for the maintenance of retail prices fixed by the company. In recent years, however, this clause has been omitted from these contracts, and the company now expressly disclaims any attempt to control the retail price charged by the dealer. The position of the International Harvester Co. is that dealers in farm machinery are not strictly its agents, although generally so called, but that they are free to do as they like in the matter of prices, subject to the right of the company to cease dealing with them if they adopt methods which tend to injure its business or demoralize the trade.

The Bureau found, however, that following the elimination from the company's contracts of the clause relating to retail prices there has been a rather general issuance of price lists in different parts of the country, usually by general agents of the company, naming so-called "suggested prices" to be paid by the farmer. These price lists are sometimes gotten out in rather elaborate form, and over the name of the International Harvester Co. of America, and they have had a rather wide circulation among dealers. Representatives of the Bureau found that such price lists had been issued by several general agencies of the company in recent years.

The assistant general manager of the company explained these price lists on the ground that there was a constant demand on the part of the company's salesmen for suggested prices, largely as a matter of information for the benefit of final purchasers who frequently made requests for quotations. In this connection he said:

There is a constant demand on the part of our salesmen for these suggested prices. . . . Some of our men have been stupid enough — indiscreet enough — to comply with this request to the extent of getting out a "suggested list." I may say, however, in justice to them that there was a period along about 1904–5 when that was recognized by our counsel at the time as not being objectionable. Later instructions were issued not to do it, as it led to a misunderstanding as to what our motives were.

It is obvious that the company could immediately stop the issuance of such lists if it genuinely desired to do so.

The company's position is that these lists have no effect and are not intended to have any effect in the direction of maintaining uniform retail prices. The Bureau, however, is of the opinion that the distribution of these lists tends to the maintenance of more uniform retail prices by deterring dealers from making concessions.

Local Discrimination in Prices and Terms

The general policy of the International Harvester Co. is one of uniform prices to dealers. Complaints were submitted to the Bureau, however, to the effect that at times it engages in local price cutting for purposes of competition. Admissions of the company show that moderate concessions are rather frequent. The Bureau found a large number of such moderate concessions and also a limited number of deep cuts, but the company itself admitted such deep cuts in only a very few instances. The company specifically denied that its policy is to make deep cuts to injure competitors. It is obviously difficult to say just where moderate concessions in prices cease to be an ordinary incident of competition and become subject to condemnation. It should be noted that the laws of several States in which the International Harvester Co. does business specifically provide against local discrimination in prices. However, the Bureau is of the opinion that such discrimination in prices has not had a serious effect on the business of competitors.

It may be pointed out that in some of its newer lines the company has adopted a general policy of distinctly low prices, which

apparently it is enabled to do because of the high prices it secures on the older lines.

In this connection there is much complaint that the company grants unusually long terms of credit to purchasers of some of these newer lines. One of the competitors of the company said, "The International Harvester Co. sells terms, not harrows." Other complaints as to the company's terms were made especially with respect to manure spreaders, wagons, and gasoline engines. The advantage of the Harvester company in this respect, because of its superior resources, is referred to elsewhere. This, however, is a matter distinct from local discrimination, although, in the opinion of the Bureau, it is more serious in its effect on competitors in the new lines, where the proportion of the company's business has been rapidly increasing.

Misrepresentations Regarding Competitors

Complaint was also made to the Bureau that there has been more or less general misrepresentation of competitors by the salesmen of the International Harvester Co. While some years ago there were a few such complaints involving misrepresentation of the financial standing of competitors by the company's salesmen, no recent complaints on this score were received.

In the opinion of the Bureau there is foundation for this complaint, but apparently the practice has not resulted in seriously handicapping competitors.

While notwithstanding the various objectionable practices above set forth the business of the competitors of the International Harvester Co. in harvesting machines has increased, obviously this is no defense of methods in themselves objectionable. Moreover, as already shown, the International Harvester Co. has thus far substantially maintained its monopolistic position in the harvesting-machine business, while in several of the newer lines in which it had no interest at its organization it has, in a short period of years, built up its business so rapidly that in some of these it now has a large proportion of the trade, and in one, manure spreaders, a majority of the business. It is also worth noting that the company's business in wagons has increased rapidly in the face of a reduction in the total demand.

Sources of the Combination's Power

Three principal factors appear, therefore, to have been chiefly responsible for the position attained by the International Harvester Co.: (1) Combination of competitors; (2) superior command of capital; (3) certain objectionable competitive methods.

The prime source of the company's power is undoubtedly to be found in the original combination of the principal competing companies in the harvesting-machine business. As already shown, the company was also able to use its position in this branch to great advantage in forcing its way into new lines.

Next to this monopolistic control of the harvesting-machine business proper is the company's exceptional command of capital.

While its financial advantage has been supplemented by the adoption of certain objectionable competitive methods, the mainspring of its power was the consolidation of the leading competitive factors in the industry.

X

THE CAPITALIZATION OF THE INTERNATIONAL MERCANTILE MARINE COMPANY[1]

THE International Mercantile Marine Company completed, on December 31, 1903, its first year of life as a going concern. Up to the date of this writing, if stock quotations are any indication of its financial condition, the success of the company, from a market standpoint, is problematical. Its preferred stock is quoted at 18 and its common stock at 5, prices which indicate a general conviction that the equity in the company is worth little.[2]

There is, however, a possibility that the stock market may be mistaken in its estimate of Mercantile Marine. In a declining market, stock values are influenced more strongly by the financial necessities of holders than by the earning power of the companies whose ownership they represent. This is especially true of the stocks of corporations launched on a declining market where the influence of every adverse factor is exaggerated. International Mercantile Marine has, in this respect, been peculiarly unfortunate. It was brought out during the fall of 1902, when the decline in the market was in full swing, and after the public buying power had been exhausted. Under the circumstances, these securities had no chance of a favorable reception. Moreover, almost from the start they were subject to inside pressure. The English venders, stimulated by some natural distrust of the unknown economies of combination, and strenuously exhorted thereto by the financial press of Great Britain, which has been

[1] From the *Political Science Quarterly*, Vol. XIX, 1904, pp. 50–65.

[2] Receivership ensued at last in 1915. The reorganization plans, now under discussion, propose to reduce the total of outstanding securities by one half. — ED.

from the outset hostile to the combination,[1] sold the stock which they received in payment for their interest, and the members of the American underwriting syndicate, as well as the American vendors, hard pressed by the continued stringency in the money market, have contributed to the selling pressure.

The proposition should be considered on its merits, without special reference to the market price of the company's securities.

The outstanding capital of the Mercantile Marine Company is divided as follows:

Underlying bonds	$16,000,000
20-year collateral debenture bonds (4½ per cent)	52,000,000
Preferred stock, cumulative (6 per cent)	54,600,000
Common stock	48,000,000
Total	$170,600,000

To pay interest and preferred dividends — common dividends, at least for some years to come, are hardly to be expected — will require the following amounts:

Interest on underlying bonds, taken at 5 per cent	$ 800,000
Interest on debentures	2,340,000
Dividends on preferred stock	3,276,000
Total	$6,416,000

Following the practice of the older German and English companies and allowing 60 per cent of net earnings for depreciation, insurance, and renewals, the total requirements, letting these funds include the sinking fund, are $16,000,000.[2]

[1] For example, the *Economist* on Nov. 29, 1902, referring to the report that certain English vendors had expressed a desire to receive bonds in lieu of cash, remarked as follows: "They (J. S. Morgan and Co.) also state that the offer was made on the expressed desire of some shareholders, who wished to invest in the bonds. If that be the case, it seems to imply a singular lack of business capacity on the part of the vendor shareholders, since they need not seek far to find securities with a much greater margin of security than these bonds to return a higher rate of interest. All they do know is that its capitalization will be enormously in excess of that of the undertakings that have been absorbed in it, and none should be better aware than themselves of the difficulty that will be met with in earning dividends on such a large sum, since they have had the experience of the same difficulty with a much smaller capitalization."

[2] The bonds of the International Navigation Company, of which $13,686,000 are outstanding, call for a sinking fund of $250,000 to $500,000 annually, beginning May 1, 1905, which will retire the bonds at maturity in 1929. No sinking fund is

Shortly after the Mercantile Marine Company was organized, the statement was made, unofficially, but apparently on good authority, by the Wall Street *Journal*, that the average net earnings of the different fleets for four years were $6,107,675. The same authority stated that the estimated savings in the cost of operation for the year were $10,000,000. Adding these to the average profits above mentioned, the earnings of 1903 should have amounted to a sum sufficient to pay dividends on the preferred stock, although it was not expected that any disbursement would be made. In other words, accepting the corporation's own estimate of the economies which can be secured by its changes in administration, the amount of its earnings falls short of the amount necessary to pay dividends on the common stock.

Before proceeding further in the analysis, let us test the accuracy of this conjectural estimate by comparing these figures with the amount actually earned by other companies during 1902, a year which was more favorable for the shipping industry than 1903. Such a comparison is presented in the following table:

	Tonnage	Net Earnings	Net Earnings per Ton
Cunard Company	114,410	$ 1,235,750	$10.80
North German Lloyd	583,042	4,392,500	7.53
Hamburg-American	651,151	4,458,198	6.85
International Mercantile Marine	1,034,884	16,107,000 (est.)	15.57

It thus appears that the estimated tonnage earnings of the Shipping trust for 1903 are nearly twice the average amount — $8.39 — which was earned during the preceding year by its leading competitors. Moreover, the German companies have for many years operated under a close pool which secures them all of the economies which the Shipping trust was organized to obtain. Unless some other factors shall be discovered by the combination to increase its earnings, these preliminary estimates will eventually require some revision.

provided for the bonds of the International Mercantile Marine Company, but they are subject to call at 105 after five years. If an adequate reserve is provided, the necessity of a sinking fund on bonds secured by shipping property does not appear.

Accepting the same figure of tonnage earnings for the Shipping trust which was attained in 1902 by its competitors, namely $8.39 per ton, we have next to inquire how the combination measures up to its interest and dividend requirements. The net earnings of the company, on this basis, would stand at $8,941,398, leaving $5,801,398 over fixed charges, for depreciation, renewals, and replacements. This amounts to about $5.60 per ton as compared with $4.30 per ton for the Hamburg-American line in 1902, $6.19 for the North German Lloyd, and $8.04 for the Cunard line. If we debit the earnings of the International Mercantile Company with $5.00 per ton for these various necessary expenses, an amount which, considering the age of their fleet and the necessity of providing for the redemption of their bonds, would seem to be no more than is required, and if we assume, as before, their tonnage earnings at $8.39 per ton, the Trust has only $606,978 remaining for its preferred stockholders. That this supposition is not wide of the truth, may be seen from the experience of the North German Lloyd Company in 1902, which earned, over interest, 14,770,000 marks, and credited to renewals and insurance all but 212,477 marks of this amount, reducing their dividend payments from 5,278,131 to 210,623 marks. Taking a three years' average of the earnings of the Cunard, Hamburg-American, and North German Lloyd companies, we find that their combined depreciation and insurance charges amount to $24,719,112 out of $37,976,794 of net earnings, or about 65 per cent. It is impossible to escape the conclusion that the Shipping trust must appropriate a similar proportion of its profits for the service of the company, if the first care of its management is for the property of the company. If this is done, however, a readjustment of the capital of the company is among the probabilities.

We have not reached the end of the chapter. The Shipping trust was organized during a period of great prosperity, when the earnings of ocean transportation, although depressed somewhat below the abnormal figures of 1900, were still large. To pass final judgment upon its financial future, it is necessary that we cast backward and discover, if possible, from the history of other shipping companies, what may be expected if earnings follow the course of former years.

In the accompanying table appears the income account of the Cunard Company for a period of twenty years, including 1883 and 1902.

CUNARD STEAMSHIP LINE

Year	Profits, Including Balance Forward	Reserved for Depreciation	Reserved for Insurance	Total Balance	Dividends	Forward	Insurance Fund Stands at
	£	£	£	£	£	£	£, Often Written lb.
1902	263,617	158,722	24,686	68,808	64,000 (4 %)	4,807	357,000
1901	226,022	167,900	5,766	65,984	64,000 (4 %)	1,984	350,000
1900	553,241	284,488	119,037	143,434	128,000 (8 %)	15,434	350,000
1899	294,856	173,223	34,247	83,527	80,000 (5 %)	3,527	260,000
1898	261,691	172,169	29,496	57,663	56,000 (3½ %)	1,663	235,000
1897	222,475	166,938	27,999	41,691	40,000 (2½ %)	1,691	212,000
1896	249,788	184,822	32,417	42,181	40,000 (2½ %)	2,181	202,000
1895	144,305	180,325	. . .	183,731[1]	. . .	deb. int. 1,466	187,000
1894	94,953	177,104	. . .	183,020[2]	. . .	2,072	230,000
1893	200,091	154,419	39,966	35,868[3]	32,000 (2 %)	3,868	322,000
1892	174,607	125,856	33,496	36,296[4]	32,000 (2 %)	4,296	317,500
1891	220,991	125,426	38,407	52,382	48,000 (3 %)	4,382	315,000
1890[5]	246,601	125,840	43,144	72,838	64,000 (4 %)	8,838	280,000
1889	350,203	130,573	{41,918 / 54,480}	175,469	96,000 (6 %)	4,988	240,000
1888[6]	314,736	{135,327 / 23,000}	{46,815 / 40,472}	130,172	64,000 (4 %)	2,700	. . .
1887	254,482	135,500	77,839	41,143	40,000 (2½ %)	1,143	Debenture debt reduced from £450,000 to £96,000
1886	160,910	137,721	23,189	nothing left	nothing left	. . .	Loss of *Oregon* costs £113,241
1885	165,943	141,506	24,437	nothing left	nothing left	. . .	140,000
1884[7]	103,948	{87,018 / 23,000}	nothing left	nothing left	. . .	. . .	117,000
1883	146,920	93,134[8]	50,094	. . .	none	1,270	150,094

[1] £39,426 from insurance fund.
[2] £88,067 from insurance fund.
[3] £30,000 from insurance fund.
[4] £25,000 from insurance fund.
[5] The company had on hand at the end of 1890 in investments, bills, and cash, £559,922.
[6] £96,000 debentures paid off July 1st. Balance of cash and investments, £205,804.
[7] £23,000 taken from insurance fund and added to sum reserved for depreciation.
[8] Depreciation fund stands at £302,000.

The feature of the movement which will immediately impress the reader is the extraordinary fluctuations of net earnings. From a minimum of £103,948 in 1884, they rose to a maximum of £350,203 in 1889, an increase of 237 per cent. From that point, although fairly maintained until 1893, they fell in 1894 to £94,953, the smallest figure ever reached. The depression continued during 1895, but in 1896 began the great upward swing which carried earnings up more than 550 per cent, to the enormous total of £553,241 in 1900. From this maximum, the decline was rapid, profits standing at £226,022 in 1901, and £263,617 in 1902. Passing over, for the time being, the explanation of these remarkable fluctuations, let us examine the disposition of profits which this company employed. We note at once that the reserves for depreciation took up a large share: £3,104,011 out of a total of £4,650,380. Another large amount, £787,905, or 16⅔ per cent of the total, went to the insurance fund, which the company has always maintained at a high figure. Out of the surplus remaining, to which was added £182,493 from the insurance fund, bringing the total amount available for distribution up to £940,957, £848,000 was paid in dividends, leaving £93,957 to be carried forward, an amount successively included in the annual profits. In other words, out of £4,650,380 of profits earned in 20 years, the Cunard Company paid out £848,000, or 18.8 per cent to its owners, and kept 81.2 per cent in the business. We note, moreover, that the disbursement of dividends was by no means regular. In six years out of the twenty, nothing was paid on the stock. In five other years, less than 3 per cent was paid, and in only one year, 1900, was as much as 8 per cent distributed to stockholders.

We note also with what extreme care the directors guarded their insurance and depreciation funds, taking every occasion of large earnings to build up these safety deposits, and refusing to sacrifice to the temporary advantage of the owners the permanent welfare of the company. In thirteen years out of the twenty, the profits of the company exceeded £200,000, aggregating £3,658,794. Of this amount only £816,000 was paid in dividends, £2,842,794 being carried to reserve. The shareholders reaped no small benefits, however, from their enforced self-

denial. In four years of the period 1892–95, the insurance fund, which is held in cash and securities, was drawn upon for dividends or to maintain the depreciation fund. Of the £64,000 paid out to stockholders during these four years, £55,000 came from the reserves.

In short, it was only by the most careful economy, by the utmost prudence and conservatism in the distribution of profits, that the Cunard Company was able, over a twenty-year period, to average 2.6 per cent to its stockholders and, during the past ten years, to earn 3.1 per cent on a capital which at no time exceeded the book value of its ships.

For an explanation of the irregularity of these profits, we turn to the nature of the industry. The shipping business is, of all industries, the most irregular. It is liable not merely to the usual alternations of prosperity and depression, but to sudden fluctuations of rates and traffic which are entirely without parallel in any other branch of trade.

To begin with, the industry is strictly competitive. The high seas can never be monopolized. Dockage facilities in the leading countries are open to the ships of all the world, and shipyards will furnish a cargo steamer at a moderate price. Under these conditions, a permanent control of the shipping industry, sufficient to maintain rates or to control traffic, is out of the question. Agreements among the regular lines may introduce a certain degree of stability into passenger rates, and into the freight charges on the higher classes of commodities, but for the great mass of traffic, the raw materials and rough and half-finished products of commerce, carriers and shippers will continue, as they have from time immemorial, to make their individual bargains, and the rates of charge will continue to be fixed by the higgling of the market.

This situation has two consequences. If at any port the supply of shipping waiting for cargoes exceeds the amount of business offered, the competition between owners will force rates down sometimes to the smallest admissible margin above operating expenses. The amount asked by the marginal ship will fix the rate for the time being for all vessels leaving the port. On the other hand, a small excess of tonnage offered will have an

equal effect in raising the rate. Some classes of commodities can be delayed in shipment longer than others, and some vessel owners can afford to lay up a portion of their tonnage rather than accept unremunerative rates. Generally speaking, however, the rule holds good. From every port and on every line of traffic, the rates are constantly changing in a way which would stagger a railway traffic manager, although he was deeply versed in the theory and practice of rebates and special concessions.

For example, take the following table of outward rates on coal from Wales to various ports in 1899:

	s. d.		s. d.	Per Cent of Variation
Port Said	7 9	to	13 6	74
Genoa	7 6	to	11	47
Aden	11 6	to	16 6	43
Bombay	12	to	18 6	54
Colombo	12	to	19	59
Cape Town	19	to	30	58
Rio Janeiro	11 6	to	16	39

The movement of grain rates from the United States, while less irregular than the figures quoted above, is also subject to wide variations.

Examples of more extreme fluctuations are easy to find. The course of rates in the British market in 1896 offers a typical illustration of the extreme instability of ocean rates. The *Economist*, in its annual review of the shipping industry for 1895, reported, at the close of that year: "The tonnage afloat is enormously in excess of the world's requirements, and so long as this continues we cannot see that there will be an improvement." During the early part of 1896, this condition of extreme depression continued. Only in outbound rates to the East, where the China-Japan troubles made a brisk demand for shipping, was any profit presented. These rates advanced, and remained on a high level throughout the year. A large number of ships, finding no profitable employment at home, went out to the East. Once there, however, and the war ended, they could not get back again, for return freights were not to be had, and it was impossible to return such a long distance in ballast without the prospect of remunerative employment. This situation left a large number

of cargo vessels stranded in eastern ports, unable to get back to western waters. A large part of the world's carrying trade was thus locked up. The available supply of shipping was suddenly diminished. The tonnage afloat accessible to English shippers was no longer as in 1895, "enormously in excess of the world's requirements."

Upon a straitened supply was now precipitated an avalanche of orders. Says the *Economist:*

The corn trade in the past year assumed a novel and unexpected position; the production of the world was slightly short of the consumptive requirements, . . . two of the large producing and exporting countries (India and Australia) being actually converted into considerable importers, and several hitherto small importers making largely increased demands.

The general trade of the country, as the *Economist* notes, maintained the improvement and expansion awakened and started more than twelve months earlier.

These combined influences came to bear on the freight market almost simultaneously; shippers of nearly every description, all wanting the same thing at the same moment, with a rather short supply of the article; result, blind competition sending up the price of tonnage by leaps and bounds, in many cases 200 to 300 per cent, from the end of September to the end of November. . . . By so much as the rise was rapid, by so much was the decline equally rapid, and at the close of the year we find freights all around, in every trade, worse if anything than at the commencement.[1]

This experience has been repeatedly duplicated in every market. It is true that the total supply of ocean shipping will in time become available to relieve any congestion; but much time must often elapse before relief can be extended, the tonnage must be moved at once, and the ship-owners who are fortunate in being on the spot reap a rich harvest. On the other hand, vessels which have gone out in ballast to Argentine or the United States, expecting full cargoes of grain, or which have made the long voyage to Australia, expecting a large movement of wool, suffer the full effects of a crop failure or a small wool clip.

The following table shows the fluctuations over a ten-year period in four of the leading items in the world's export trade.

[1] Commercial History and Review of 1896. *Economist*, Vol. LV, supplement, p. 25.

Year	Export of Wheat from U. S. Bushels	Per Cent of Change from Previous Year	Export of Cotton from U. S. Bales	Per Cent of Change from Previous Year	Export of Corn from U. S. Bushels	Per Cent of Change from Previous Year	Export of Wheat from Russia Thousand cwt.	Per Cent of Change from Previous Year
1892	225,665,812		5,858,000		76,602,285		26,297	
1893	191,912,635	− 15	4,390,000	− 27	47,121,894	− 39	50,351	+ 91
1894	164,283,129	− 14	5,232,000	+ 19	66,489,529	+ 48	65,966	+ 31
1895	144,812,718	− 12	6,726,000	+ 29	28,585,405	− 57	76,453	+ 16
1896	126,443,968	− 12	4,627,000	− 31	101,100,375	+243	70,774	− 6
1897	145,124,972	+ 15	5,979,000	+ 29	178,817,417	+ 77	68,670	− 2
1898	217,306,004	+ 49	7,540,000	+ 26	212,055,543	+ 19	57,047	− 15
1899	222,618,420	+ 2	7,313,000	− 3	177,255,046	− 17	34,466	− 40
1900	186,096,762	− 17	5,946,000	− 19	213,123,412	+ 20	37,627	+ 9
1901	215,990,073	+ 15	6,538,000	+ 9	181,403,473	− 20	44,626	+ 19

Many of these fluctuations took the shipping trade by surprise, and either too few or too many boats were available. In other cases, the supply of shipping the world over was either excessive or redundant, and freights fell or rose to correspond.

So much for the temporary fluctuations of ocean freight rates and tonnage. There are also movements of longer duration, corresponding to the ebb and flow of general business, but subject in peculiar measure to the influence of special forces. From 1893 to 1897, for example, the leading commercial countries were suffering from a commercial depression which caused a general decrease in the tonnage of international trade, and a still greater fall in the value of exports and imports. The effect of this situation upon the shipping industry has been already indicated. Tonnage could not be decreased, and, in fact, the tonnage of the world during these three years increased. The result was an unprecedented depression in the shipping industry. In 1893, the *Economist's* review reports a large number of steamers laid up and a number disposed of at forced sale. In 1894, the report was "low, unprofitable freights and declining values of property engaged; the whole of the enormous trade has brought little or no profit, and a very bare margin over working expenses, far from enough to cover depreciation." In 1895, came a year "which will not readily be forgotten by the ship-owners. . . .

Our anticipations have been to the full realized, and probably a worse year than the present has not been experienced by the very oldest in the business."[1] The condition of the trade, in 1896, as already remarked, was little better.

During the four succeeding years, the situation was entirely changed. The widespread industrial revival caused a large increase in the value of foreign trade; and the shipping trade, as illustrated by the rapid and extraordinary rise in the profits of the Cunard Company, became very profitable.[2] The main support of the market, during 1897 and 1898, was the American export trade, which was characterized in the *Economist's* annual review of 1897 as follows:

It contributed largely toward sustaining rates in the early months, and causing a material advance during the autumn and late summer in all other rates by the ready absorption and continued demand for tonnage of all descriptions from the leviathan 8000 to 20,000 ton cargo boats, to small fruit steamers.[3]

In 1899 the advance continued. General trade, the world over, was active, and the South African war resulted in the largest withdrawal of shipping that had been known for more than a generation. An outbreak of hostilities, involving even a second-rate power, always demands the services of a large amount of shipping. Even the effect of the Greco-Turkish war was sensibly felt; the influence of the China-Japanese war has been already mentioned; and the Spanish-American war materially contributed to the prosperity of the trade in 1898. The shipping industry can, over a period of years, depend with reasonable certainty upon the assistance of several wars. If international disturbances occur during a period of depression, the freight and traffic situation is relieved, and if, as in the case of the Boer war, the outbreak of hostilities comes hard upon the heels of general and abounding prosperity, the result is enormous

[1] *Economist*, Vol. LIV, supplement, p. 26.

[2] The combined exports and imports of the United States, Germany, and Great Britain, in 1895 were valued at $6,323,207,441. In 1901, six years later, their value had risen to $8,635,362,581. A large portion of this increase was undoubtedly due to the rise of prices, but the gain in tonnage was chiefly responsible.

[3] *Economist*, Vol. LVI, supplement, p. 24.

profits for all ship-owners. Not only does war increase the demand for ships, usually on terms highly favorable to the owners, but it raises the level of freight the world over by reducing the supply of tonnage.

These results followed from the South African conflict. At the close of 1900, the British government had withdrawn some 2,000,000 tons of shipping, an amount nearly equal to the total steam tonnage of Germany, and nearly double that of France. In 1900, moreover, the troubles in China required the transportation of large numbers of troops to the East, and throughout the Boer war, a large coal tonnage was kept moving to the Cape. The result, as stated in the *Economist's* annual review, was that

> The tonnage taken on time charter for all trades during the past year has been unprecedented. The rates paid by our Government for transports were 20*s*. per gross register per month, and in some cases more. Many charters in ordinary trades were made for long periods at very remunerative rates. Modern boats have commanded from 7*s*. to 11*s*. 6*d*. per gross ton, according to the trade and length of charter.[1]

In 1901, however, the tide turned. During the preceding four years, the supply of tonnage had been increased 4,049,260 tons, and with the close of the war, the British government rapidly released the ships which it had employed. To make matters worse, the American corn crop was a failure, and the industrial depression on the continent reduced the amount of freight movement. Rates fell 30 per cent throughout the year, and have continued to fall during 1902 and 1903, the close of 1903 finding the trade extremely depressed, with little prospect of early improvement.

We find in this hasty review of the recent history of the shipping trade an explanation of the irregularity of the profits of the Cunard Company, and can understand why the directors have pursued such a niggardly policy in the disbursement of profits. The management of a shipping company lives in constant apprehension. Exposed to increasing competition on every hand; compelled every year to build new and larger boats to keep pace

[1] *Economist*, Vol. LX, supplement, p. 28.

with their rivals; anxiously scanning the commercial horizon for signs of business depression, crop failures, famines, or labor disturbances; hoping and scheming for a few crumbs of subsidy, to introduce a modicum of fixed income into their earnings; engaged in a business as shifting and unstable as the sea on which that business is conducted — is it any wonder that the experienced ship-owners hold fast to their profits and regard the results of a year like 1900 as a gift of Providence to be guarded with zealous care?

Into this peculiar business came the promoters of the International Mercantile Marine Company. Attempting to apply to the shipping industry, the same principles of consolidation and capitalization which had been superficially successful on land, they imposed upon the new corporation an unusually heavy burden of capitalization, and they so arranged the capitalization as to make conservative financial management of the new company very difficult. The purchase price of most of the subsidiary companies was based on the profits of 1900. In the vendors' agreement between the syndicate and the White Star line, for example, it was stated that

> the valuation of the said shares hereunder and under said principal contract shall, subject as hereafter provided, be a sum equal to ten times the net profits of the company of the year 1900, subject to the following exceptions . . . (*a*) a sum for depreciation equal to 6 per cent on the amounts at which the property of the company stood on its books on the first day of January, 1900, and a sum for insurance . . . equal to £3 10*s*. on the same amount . . .[1]

It was further stipulated that the earnings of steamships employed by the British government should "be credited . . . with net earnings of the same amount as were earned or would be earned by similar steamships of the company for the same periods in their ordinary trades."

The year 1900, as has been shown, was one of abnormal profits. The Cunard Company nearly doubled its net earnings, and it is reasonable to suppose that other companies were equally

[1] For the text of these vendors' agreements, see Report of the U. S. Commissioner of Navigation, 1902, Appendix T, pp. 380 *et seq.*

fortunate. A partial record of the prosperity of this year is furnished by the record of dividends. The average dividend of twenty-five leading companies in 1896 was 6 per cent; in 1898, 7.7 per cent; and in 1900, 9.4 per cent. In the extract from the vendors' agreement quoted above, we find a recognition of the fact that the profits of 1900 were exceptional, viz., the provision reducing the earnings of ships employed in the government service to the general average of private employment. This reservation, however, does not go far enough. The mere fact of a large government employment, as has been shown, was sufficient to heavily increase the earnings of ships in private employment, and in capitalizing the earnings of this single year, the promoters of the Shipping trust made a serious mistake.

Indeed, so apparent was the mistake, and so clearly did the trade foresee that reaction was impending, that this fact was openly urged upon the shareholders by the Leyland line as an inducement to fall in with Mr. Morgan's plans. Said Mr. Ellerman, in May, 1901, at the shareholders' meeting of Frederick Leyland and Company:

> The outlook for freights in the near future is, in my judgment, an uncertain one. We have had prosperous times, and I feel that the near future may bring, at all events for a time, a reflux of bad times, particularly when the tonnage which is usually employed in the North Atlantic trade, but which is now employed in government transport work, returns to normal employment; in addition to which a large amount of tonnage is building in America for employment in the Atlantic trade . . .[1]

Not only was the amount of capitalization excessive, but what was more important, the arrangement of the capital of the Shipping trust, taken in connection with the amount of the different issues, was open to serious criticism. In addition to an amount of bonds fully sufficient to absorb the maximum earnings of the company, a liability of $54,600,000 of cumulative preferred stock was assumed, all of whose passed dividends must be paid before the common stock receives anything. Our previous discussion has shown the shipping business to be so irregular that even with

[1] Report of Commissioner of Navigation, 1901, p. 321.

the most moderate capitalization, in some years dividends must be passed, and in other years paid out of reserve. At all times, the directors should have a free hand in determining whether profits shall be distributed to stockholders, used for replacements and depreciation, invested in securities, or held in cash. The irregularity of the business is so great, that a free disposition of profits to stockholders is out of the question. The policy of a well-managed shipping company is dominated by the necessity of reserving from two-thirds to three-fourths of the profits in order that one-fourth may be paid out in dividends. In view of this fact, the absolute amount of the Shipping trust's capitalization is of much less consequence than the nature of the liabilities which it includes. The fact that the company is excessively capitalized is of less consequence than the fact that the arrangement of this capitalization is such as to make prudent financial administration very unpopular with stockholders. In this arrangement, fixed charges and obligatory payments predominate. Of the $170,600,000 of capital, $122,600,000 consist of bonds and cumulative preferred stock. If the debenture interest is passed, while the form of the bonds puts foreclosure proceedings out of the question, the unpaid interest must be discharged before anything is paid on the preferred stock; and if the preferred stockholder is forced to await the convenience of the corporation, the hope of the common stockholder of receiving anything on his investment becomes remote. In other words, a conservative administration of the finances of the shipping consolidation involves a series of postponements, an accumulation of deferred claims. The collection of a reserve sufficient to pay dividends in years of depression, if we may judge from the experience of other companies capitalized on a basis similar to that of International Mercantile Marine, is likely to be seriously interfered with by the importunities of deferred claimants.

It would be going too far to say that the International Mercantile Marine Company is a failure. Its future lies in the hands of the stockholders. If they will sanction a policy of conservatism in the distribution of earnings there is no reason to suppose that the preferred stock of the company may not eventually be raised to the rank of an investment. The unfortunate experience of

the corporation up to the present time, however, emphasizes the fact that it is necessary, in arranging the capitalization of a new company, to take into careful account the conditions of the business in which the new concern is to operate, and in every case to assume that industrial history is to be repeated. The "economies of combination" are no doubt considerable, but they are too problematical to be safely included in an estimate of earnings available for distribution to stockholders.

EDWARD SHERWOOD MEADE

XI

THE UNITED STATES LEATHER COMPANY[1]

CHRONOLOGICAL SUMMARY

1892. Agreement not to wet hides for six months.
1893. Organization of the United States Leather Company.
1899. Plan for paying accumulated dividends first suggested.
      First plan of reorganization unsuccessful.
1902. Revaluation of company's timber lands.
1903. Second plan of reorganization unsuccessful.
1904. Final plan of reorganization proposed.
1905. Announcement of successful operation of plan.
      Incorporation of Central Leather Company.
1906. Attempted merger of the two companies.
1907. Beginning of the Colgate litigation.
1909. Decision of the New Jersey court against the merger.
      Final settlement of litigation out of court.

THE reorganization of the United States Leather Company into the Central Leather Company affords one of the simplest and most instructive examples of modern reorganization finance. The financial difficulties of the company grew out of the highly competitive character of the leather industry combined with the need of an abundance of working capital which the tanning of hides on a large scale requires. To these economic conditions was added the fact that the preferred stock, carrying heavy preferential dividends, was issued largely to acquire unproductive timber lands. The reorganization itself involved the question of the rights of preferred shareholders to accumulated but unpaid dividends and to a bookkeeping surplus arising out of the supposed increase in value of tangible assets.

The sole leather industry does not lend itself readily to large-scale production. Little capital for plant is required, in proportion to the output; the raw materials (hide and bark) are purchased in a highly competitive market, and the finished product is sold under equally keen conditions of competition. The

[1] From A. S. Dewing, Corporate Promotions and Reorganizations, Harvard Economic Studies, 1914. This chapter is only one indication of the wealth of material gathered therein. Copious footnotes are omitted.

American tanners buy their raw Argentina hides in competition with Canadian and European tanners, and they sell their leather in competition with the leather of these same tanners. The markets in which they buy and sell are, therefore, world-wide in scope. No large amount of skilled labor of a technical order is required, for the tanning of hides is a long-time process in which the cost of labor is subordinate to the cost of the raw material. The small tanner who is near his bark lands can, indeed, tan a few hides a week quite as cheaply as the large tanner, further removed, can tan a hundred or a thousand times as many. Under these conditions it would seem that American tanners could derive little advantage from consolidation. Yet, in spite of these underlying facts, the sole leather industry was one of the first to resort to centralized organization in the hope of allaying the disastrous results of competition and enhancing the profits through large-scale production. At the time this consolidation was formed, moreover, it was represented by the only corporation in the country with a capitalization well over a hundred million dollars. Viewing the matter broadly, then, we seem to have here a huge capitalistic combination seeking to apply the methods of large-scale production without the prop of a natural or legal monopoly and in the face of those economic conditions which favor small-scale production.

A considerable part of the heavy sole leather of the country is tanned in Pennsylvania and southern New York State. Near are the large hemlock and oak forests which yield the bark upon which the tanning industry depends. For a considerable period of time, until perhaps 1880, the tanners experienced no difficulty in obtaining all the bark they needed at nominal prices. Gradually, however, as the more available sections of forest land were cut, and the bark became dearer, the tanners themselves began to acquire extensive areas of timberland in order to safeguard their supplies. Each tanner bought the land as it was offered without much regard to the question of whether it was nearer his own tannery or that of a competitor. As a result the various timber holdings became so intermingled that economical exploitation of the bark lands was impossible. The price of sole leather fell steadily from 1884 to 1891, and competition among

the tanners grew increasingly severe. In 1892 there were signs of marked over-production. As a result the large tanners entered into an agreement not to wet any more hides for a period of sixty days. The plan worked excellently and the tanners were able to dispose of their surplus stocks without suffering a loss.

The favorable outcome of the agreement of 1892 and the widely recognized success of the oil, whisky, and sugar combinations led five of the largest tanning interests to consider the possibility of making a more economical use of their bark lands by merging their different interests in one company. The bark for each tannery could then be obtained from the nearest source, — obviously an economy of operation, — and with the control of a large proportion of the available bark, with economical methods of manufacture and decreased selling expenses, the tanners believed they would be able to produce leather more cheaply than their competitors. Then, too, some of the older men were desirous of organizing their business affairs so that their estates could be administered easily in case of their death. These were the chief reasons which led to the formation of the United States Leather Company in the spring of 1893.

The leaders of the movement appointed committees to appraise the tanneries and bark lands owned by the interests that had consented to enter the consolidation. The property was then acquired by the consolidated company on the basis of the appraisals by issuing $100 in preferred stock and $100 in common stock in return for each $100 in the appraised value of the property. In other words, the company paid for the tanneries and bark lands by issuing its preferred stock and by giving an equal amount of common stock as a bonus. In this way the leaders of the movement acquired approximately 110 tanneries, controlled by some 60 leather houses. Besides the tanning properties the combination acquired about 400,000 acres of bark land and the bark rights on nearly 100,000 more. At the outset, the combination controlled approximately 72 per cent of the country's output of hemlock tanned leather, about 30 per cent of the oak tanned and about 45 per cent of the union tanned leather. From various lines of evidence it appears that the strongest firms in the hemlock branch of the industry went into the combination,

but the more prosperous oak and union tanners refused to enter, largely because they were not offered sufficiently liberal terms. It is fair to say that the United States Leather Company controlled, at its inception, about 58 per cent of the sole leather tanned in the country. No promoter was instrumental in forming the consolidation. Even bankers were not resorted to except for the sale of a small issue of debenture bonds. The formation of the company may be looked upon, therefore, as typical of those cases in which manufacturers themselves united their businesses in the hopes of obtaining the economies of combination, and large-scale production.

The United States Leather Company was incorporated in New Jersey, February 25, 1893, under the old "Act Concerning Corporations" approved April 7, 1875. The certificate of incorporation was afterward amended several times. The important items of its early financing can be expressed in a nutshell as follows. The authorized capital consisted of $64,000,000 preferred and the same amount of common stock. Of these amounts there were issued, after various adjustments had been made, $62,282,300 of the preferred and $62,882,300 of the common. The preferred stock carried 8 per cent cumulative preferential dividends, to be paid from the net earnings of the business. This was preferred both as to dividends and to assets in case of liquidation. Working capital was furnished by an issue of $10,000,000, debenture bonds of which $6,000,000 were underwritten and issued at par through a syndicate managed by Heidelbach, Ickelheimer and Company; 4 per cent of these bonds were to be retired each year at not over 110 per cent. The preferred stock was issued as has been said in return for the property of the various subsidiary tanners. With each share of the preferred stock was given a single share of the common and $600,000 par value of the common stock was also given to the syndicate underwriters as a 10 per cent commission for underwriting the debenture bonds. Using the figures derived from the appraisals, it would appear that the United States Leather Company was possessed, at its inception, of property to the value of $63,000,000. Distinctly different opinions exist as to whether the appraisals were fair. The tanners who sold their property to

the company considered them just, whereas tanners not within the combination considered them clear inflations of the actual value of the property. The greater part of the property consisted of bark lands. These were acquired on a basis of $2.50 a cord for lands bought outright and $.50 a cord for lands with bark rights alone. These bases appear from other lines of evidence to be just. There may have been an overvaluation of the tannery property. All things considered, however, it seems fair to believe that the property acquired by the United States Leather Company had an actual market value of $60,000,000, including the $6,000,000 in money obtained from the bankers. Against these assets the company issued $131,000,000 of securities, for nearly half of which the tanners admitted there was nothing tangible. The charges, including the cumulative dividends, required $5,342,584.

The financial position of the United States Leather Company with respect to other capitalistic combinations of the time deserves some comment. At its formation in 1893 it had the largest book capitalization of any American industrial corporation. The component companies of the recently dissolved Standard Oil Trust had at that time a little over $102,000,000; the American Sugar Refining Company had an authorized capital of $75,000,000; the National Lead Company a little less than $30,000,000; the American Tobacco Company $35,000,000; and the United States Rubber Company $50,000,000. All the other industrial combinations then in existence had yet smaller capitalizations.

The capitalization figures of the United States Leather Company express the unbounded optimism with which the leaders of the enterprise entered into the work of managing the new combination. The old leather interests, represented by men who had conducted their separate businesses for thirty years and more under conditions of free competition, believed that the low price of the finished product was directly attributable to the severity of competition. They confidently expected that when the economies of combination had been introduced, a period of high prices and trade prosperity would necessarily follow. According to a prospectus issued at the time the company was

formed, the constituent tanners had been making net profits of over $4,800,000. This statement was made in face of the fact that the business had been demoralized for two and a half years preceding. In addition the tanners believed they would achieve large economies by reducing the number of salesmen and sub-agencies and by closing the tanneries less advantageously situated. In spite of these economies, however, the immediate result of the combination was failure. During the first year of its history the United States Leather Company showed a net loss of approximately $1,340,000. Subsequently its net earnings increased, but in no year of its history did they warrant the declaration of the full 8 per cent dividend on the preferred stock which the original contract between the corporation and its stockholders required. In 1895, the company paid 6 per cent. Rumors were circulated, as an "unauthorized assertion by one of the directors," — that the preferred would soon be put on the full 8 per cent basis. The following year, instead of this, the preferred shareholders received merely 1 per cent.[1] Needless to say, no dividend was paid on the common stock.

[1] The following table indicates the amount of dividends paid, the earnings, and the accumulated unpaid dividends from the beginning of the company. The earnings represent net earnings applicable to dividends, after the payments of interest on debentures. It is assumed that the payments to the sinking fund of the debentures represent a proper charge to depreciation and may therefore be deducted before determining gross earnings. The dividends were cumulative from May, 1893, which accounts for the fractions.

Year	Earnings	On Pref. Earned %	On Pref. Paid %	Amount Paid on Pref. Stock	Accumulated Div. on Pref. Unpaid
May 1, '93 to Apr. 30, '94	− $1,340,494	− 2			
May 1, '93 to Dec. 31, '94	+ 726,473	1.1			
1895	9,359,833	15	6	$3,736,938	
1896	− 2,017,037	− 3	1	622,823	$21.33
1897	3,237,372	5	4¾	2,958,409	25.33
1898	1,821,921	3	4	2,491,292	28.33
1899	4,947,601	8	5	3,114,115	31.08
1900	2,281,511	3	6	3,736,938	33.08
1901	5,888,455	9½	6	3,736,938	35.08
1902	4,595,589	7	6	3,736,938	37.08
1903	1,086,095	1½	6	3,736,938	39.08
1904	3,645,267	6	6	$3,736,938	41.08
Total to Jan. 1, 1905 (Time of reorganization)	$35,573,080	—	—	$31,608,267	
1905	6,178,457	10	6	3,736,938	43.08
	$41,751,537	—	—	$35,345,205	

Total surplus from net earnings at time of reorganization, Jan. 6, 1905, $3,964,813.

The failure of the Leather company to earn the expected dividends, coupled with its heavy capitalization, gave both the common and preferred stocks a highly speculative character. During 1894 the market price of the preferred stock ranged, with considerable fluctuation, about $60 a share. The following May, because of the somewhat larger earnings, and also the wide circulation of that "unauthorized assertion of one of the directors" that the full 8 per cent would soon be paid, the price of the preferred stock reached almost its par value. This was the highest point the stock attained until the time of the reorganization of the company nearly ten years later. In 1896 the company was operating its tanneries at a loss and the market price of the preferred stock declined to about $40 per share. During this period the common stock had a mere nominal quotation of $5.

In the years immediately following, the stocks of the Leather company were little more than speculative dice for Wall Street. The failure of the preferred stock to receive the full 8 per cent dividends, any unpaid balance being cumulative, gave that glamour of the unpredictable upon which stock speculation thrives. The common stock had hardly this interest. Speculation is most active in low-priced, non-dividend paying securities, but even these must have some pretense to value, either actual or potential. The common stock of the Leather company had neither, apparently. Issued as a bonus to the holders of the preferred stock it was offset, in every balance sheet of the company, by the highly suggestive phrase "good-will, etc." Any potential earnings it might ever have had were rapidly absorbed by the constantly accumulating load of unpaid dividends on the preferred stock. Its only possible value lay in the voting power it carried, and this was merely nominal, as the control was closely held by the original leather interests. The only exception to this dead level of neglect in the eleven years during which the common stock was quoted on the New York Stock Exchange occurred in November, 1899. Ordinarily the stock had been quoted within a narrow range between $5 and $10 per share. During October of that year it assumed increasing speculative activity until on the 25th its market quotation rose to $25 a share and on the 6th of November to $40.87. Two days later it fell back to $20 a

share, and by November 29th it was again quoted at $10 a share. During this brief period the original leather interests disposed of the greater part of their holdings of common stock, reserving for themselves and their families only the preferred stock.[1] The episode was caused by an attempt on the part of James R. Keene to "corner" the floating supply of the stock.[2] The leather interests in control of the company had nothing to do with this episode and were annoyed at the time by the sudden activity of their security.

This history of the sole leather combination to 1899 is in sharp contrast to the optimism of its promoters. If one were asked to uncover the fundamental causes which explain the contrast, one would give three important reasons for the failure of the company during the first years of its history.

The most potent causes for the early failure of the Leather company lay in the general business depression which prevailed immediately after its formation. The company began its life only two months before the failure of the National Cordage Company seriously injured the confidence of people in industrial combinations, and only four months before the crisis of 1893 reached its most critical stages. The first four or five years following the panic of 1893 showed marked industrial stagnation. It is certain that, had the tanners recognized the full significance of the ominous signs in the business world they would not have formed the consolidation at that time. The relatively long time required for the manufacture of leather aggravated the difficulties resulting from the depression. Between the purchase of green "packer" hides in this country and the actual sale of

[1] The speculative character of this episode is illustrated by the large volume of sales. There were outstanding 628,823 shares of common stock. During the week from June 3 to 10, 1899, a fair illustration of the normal market, 350 shares were sold. During the week November 4th to 10th, 545,995 shares were sold, — nearly the entire issue of stock. November 7th was a holiday, so this represented an average market of 109,199 shares a day, for a stock which, six months before, had averaged about 50 shares a day. In the three weeks from October 21st to November 10th, 1,403,330 shares were sold, over twice the outstanding stock.

[2] It was generally believed by the officials of the Leather company that Keene was acting for one of the Rockefellers who had become impressed with the potential value of the company's bark lands and wished to acquire a large interest in the company.

the finished leather to the domestic consumer, from six months to a year elapses; and between the purchase of Argentina hides and the settlement with the foreign consumer this period may be extended to a year and a half. At a time of falling prices, like that of the middle nineties, the price of hides lags behind that of leather. As a result the company found itself repeatedly compelled to sell leather for less than its cost of production. It was embarrassed, in the second place, by the large amount of unproductive assets for which it had issued its preferred stock. Part of this preferred stock was represented by bark which it had taken over in the expectation of an increase in business. When the expectation was not realized the heavy stock of bark acted as a dead weight upon the company. The bark lands, too, represented an investment upon which 8 per cent in dividends were accumulating, yet they were without value until the company could command enough remunerative business to warrant their use. In a very real sense the company was "land poor." A third reason for lack of success lay in the competitive conditions of the tanning industry. Competition was inevitable and the small well-equipped tanneries were in a strongly intrenched position. This competition was not eliminated through the combination, as its promoters had hoped. The prices of leather were fixed on as competitive a basis after its formation as before. From the beginning the Leather company feared the large, independent oak and union tanners, who controlled more than half the domestic output, since the oak and union tanned leather was quite largely consumed in the American market. The independent tanners had on their side the advantages of small-scale production and direct personal supervision over the process of manufacture. Even in the hemlock branch of the industry, where the United States Leather Company was dominant in this country, conditions were hardly less competitive. A very large part of this hemlock leather, made from Argentina hides, was exported to European markets where the American interests met the output of foreign tanners.

From the formation of the leather combination, dividends in arrears on the preferred stock accumulated. It was natural, therefore, that various efforts should be made which looked

toward the adjustment of these dividend claims. During a period of eleven years, beginning in the early part of 1899 and extending until the settlement of the Colgate suit in the winter of 1910, the Leather company was struggling to rehabilitate itself from the load occasioned by these claims. Four plans of reorganization were successively proposed and three were widely circulated. All but the last met with utter failure. The fourth plan of reorganization accomplished the desired end only after long protracted court litigation. In it, however, we are presented with one of the least complicated reorganizations in the recent history of corporation finance. It is this simplicity which makes the United States Leather Company reorganization important as a type of industrial readjustment.

The first plan of adjustment of which any rumor reached the financial world was proposed in the early part of 1899. At this time the preferred stock itself was quoted about $75 a share and the accumulated unpaid dividends amounted to about $30 a share. The plan was to give to the preferred shareholders 10 per cent of script in lieu of their claims to dividends. This proposition to pay the claims of a favored class of shareholders by script offers the simplest kind of an adjustment of a contingent liability. The only question that could arise would be as to the amount of the script. The preferred shareholders would demand the full face value of their claims; the common shareholders would naturally refuse this demand on the ground that the preferred shareholders, favored though they might be, were still stockholders, not bondholders, and, therefore, under an implied obligation to bear some of the burden of an enterprise which proved less successful than had been expected. Whether or not because of this difficulty, the plan failed in this instance. It was not even presented to the stockholders. Still, in many respects, it was fairer to all concerned than any of the subsequent plans. It recognized the justice of the preferred stockholders' claim, and in the attempt to satisfy this claim it worked no hardship on the corporation itself, nor did it involve the sacrifice of any nominal though perhaps unreal rights of the common stockholders. No heavy reorganization expenses were involved. Its great defect lay in its failure to guard against difficulties

arising from further accumulations of unpaid dividends in the future.

In this last particular the second plan of adjustment was a great improvement. On August 22, 1899, a committee was appointed by the Board of Directors "to consider the question of the settlement of back dividends on the preferred stock of the company and the extinction of the cumulative clause."[1] This committee was appointed a short time after the first plan was given up and the two attempts at adjustment were part of the same undertaking. The committee reported to the Board on the 4th of October, proposing that the preferred shareholders (1) surrender all claims to dividends already accumulated, (2) agree to the abolition of the cumulative element of their contract, (3) accept a non-cumulative dividend of 6 per cent; and that in consideration of these concessions the common shareholders relinquish 50 per cent of their holdings to the owners of the preferred stock. These provisions were embodied in a circular submitted to all stockholders under date of October 10, 1899. After giving an outline of the plan the circular goes on to state that the Directors recommend its acceptance because of the growing burden of cumulative dividends on the preferred stock, which "tends to injure the good name of the company and is unjustly prejudicial to the stocks as investment." It is further suggested that it might be desirable that the common stock should have "a prospect of more immediate dividends." At this time the Directors held large amounts of common stock. Furthermore, it was urged that the removal of the cumulative feature on the preferred stock and the reduction of the dividends to 6 per cent would prevent any similar trouble in the future.

This plan, like the first one, failed utterly. Out of 622,694 shares of preferred stock only 180,165 approved; out of the 628,694 shares of the common only 43,429 approved; — less than a third in one case, and less than a tenth in the other. At first glance it seems as though the plan favored the preferred share-

[1] *Colgate* v. *U. S. Leather Co.*, Chancery in N. J., Hoyt affidavit, p. 3. Reference is here made to the documents in the suit covering the reorganization into the Central Leather Company. These documents afford excellent sources of material covering the various plans of reorganization.

holders. This was not the case. The common stock was worth, during October, about $11 a share. The holder of a share of the preferred stock was, therefore, giving up over $30 in accumulated unpaid dividend claims, relinquishing his charter rights to 2 per cent dividends each year and the cumulative feature attached to the remaining 6 per cent, and in return receiving an amount of common stock which he could sell on the market for $5. The lapse of the plan was due probably to the unwillingness on the part of both classes of stockholders to face the fact that the enterprise was, when gauged by the hopes of the promoters, a failure. In the autumn of 1899 the second great wave of extravagant optimism in regard to industrial combinations was rapidly reaching its height. Then, too, in the present instance, an adjustment of actual rights was difficult. No fraud could be urged on either side. Yet the preferred shareholders held to the wording of their contract, Shylock-like demanding their accumulated dividends though there was nothing with which to pay them; and the common shareholders, never having received a cent in dividends, regarded the whole affair as a snare, and were unwilling to relinquish any of their nominal rights, even though the actual value of their holdings would clearly be increased. The investor in corporation stock, especially the small investor whose knowledge of the management is indirect, will always gauge the value of his property by nominal rights and legal fictions rather than actual economic value. No reorganization in the entire history of our railway and industrial finance, which involved a readjustment of interests, was ever regarded as fair by all. The most glaring defect of the plan lay in the fact that the capital liabilities were not reduced. With over $130,000,000 of outstanding securities the company showed average net earnings from its formation to January 1, 1899, of approximately $2,675,000[1] per annum or about 2 per cent on the total capital. Had the committee proposed to cancel altogether half of the common stock instead of giving it outright to the preferred stockholders, the plan would have conformed better to the conditions. It would have been simpler, too, as it would have involved a sac-

[1] Including interest on debentures, an average of $2,676,804.

rifice on both sides instead of an attempt to balance one set of rights by another.

For some time after the failure of this plan nothing was done toward the readjustment of the financial affairs of the company. A dividend of 6 per cent was earned and regularly paid on the preferred stock. The accumulated unpaid dividends increased, therefore, at the rate of 2 per cent annually. During the latter part of 1902 the management became interested in the reappraisal of certain large areas of hemlock bark lands. These timber forests were bought from the old leather interests early in 1893 at what was then a fair market valuation. During the following ten years the value of both timber and bark had increased considerably. It was natural, therefore, to suppose that the lands were worth more than when acquired.[1] A revaluation was accordingly made by certain executive officers and was reported to the Board of Directors on May 28, 1903. The Committee reported that the bark property was worth about $14,000,000 more[2] than the figures at which it was carried on the company's books. This revaluation plays a considerable part in the subsequent financial history of the company. About the same time the officers of the United States Leather Company caused to be incorporated the Central Pennsylvania Lumber Company, a very large majority of the stock of which — apparently all except directors' qualifying shares — passed directly into the treasury of the Leather company. This Lumber company took over the timber but not the bark rights on the revalued bark lands. In payment for the timber the Lumber company then issued to the subsidiary tanning companies $10,000,000 of first mortgage bonds. These bonds were transferred by the subsidiary companies to the treasury of the United States Leather Company — the holding company — in liquidation of dividend claims or claims for money advanced.

[1] The reason for this reappraisal was the desire on the part of the managers, who then controlled the preferred stock largely, to adjust the accumulated dividend claims on the basis of a hidden but unearned surplus. Preferred Stockholders' Circular, May 28, 1903. Also *Colgate* v. *U. S. Leather Co.*, Hoyt affidavit, p. 14.

[2] $14,235,198.10. *Colgate* v. *U. S. Leather Co.*, Plum, Additional affidavit, p. 7.

On the same date that the report upon the revaluation of the bark lands and the formation of the Lumber company was received by the Board of Directors, that body issued a circular to the stockholders which embodied a new plan of reorganization. In this it was suggested that some of the surplus brought to light by the revaluation of the timber be used to liquidate the claims of the preferred stockholders to accumulated dividends by that time amounting to $37 per share. In detail the plan required the deposit of the preferred stock with the Morton Trust Company against negotiable certificates. The Trust thus created was to be administered by a self-constituted committee, drawn directly from the large holders of preferred stock who were then important on the directorate. It was to expire by limitation in ten years unless reconstituted by 80 per cent of the holders of the certificates. It could also be terminated on sixty days' notice by a majority of the certificate holders. The objects of the trust, as explicitly defined in the Trust Agreement, were to ratify the issue of the $10,000,000 lumber bonds, and to devise a plan whereby some of the surplus resulting from the revaluation could be divided among the preferred stockholders, in consideration of their claim to dividends in arrears. The intent of the plant to use this surplus to meet the claims of the preferred shareholders was explicitly stated in Article III of the trust agreement, so that as late as 1903 the directors were of the opinion that the increase of assets due to the higher market price of timber could be regarded as net surplus legally applicable to the satisfaction of the claims of the preferred shareholders. The point is important because in the litigation which followed the successful reorganization of the company the point was denied by some of these same men who had earlier made the proposal.

This plan failed, like the two preceding ones. Its adoption required a deposit of at least 80 per cent of the outstanding preferred stock,—upwards of 500,000 shares. On December 23 the committee announced the lapse of the plan, since only 243,728 shares had consented to the Agreement. The reasons for the failure of the plan of 1903 lay in the conditions under which it was proposed. In the broad purpose of rehabilitating the credit of the company no possible fault could be found. The plan,

unlike the preceding one, involved no balancing of rights between preferred and common shareholders. It demanded no pecuniary sacrifices, no reorganization proceedings in the broad sense of the term. Yet the trust created by the preferred stockholders was to be administered under most exacting conditions. Title to the stock was to pass to the Trust company under an Agreement the actual workings of which were controlled absolutely by a small committee in the management of the Leather company. Beneath the outward form of the Agreement there was involved the actual surrender of the rights of the preferred shareholders with no certain assurance that these rights would be protected by the trustee. Nor did the Agreement stipulate that the Morton Trust Company should obtain a settlement of all the dividends in the arrears. It was merely required to pay over to the registered holders of the beneficiary certificates 6 per cent per annum, and so much more, after deducting expenses, as the Leather company saw fit to pay over to the trustee. The Agreement, owing to the phraseology of the original certificate of incorporation, required at the outset the assent of over 80 per cent of the preferred stock; it could be maintained for ten years by the approval of 50 per cent. The management, who were to operate the Trust through their own committee, could easily control this amount. In brief the plan had primarily in view the acquisition of control of the preferred stock through the medium of a voting trust. This was less emphasized than the intention of adjusting the accumulated dividends.

The managers, being large holders of preferred stock, were actively in favor of this Agreement. They believed confidently that the reorganization would go through. In view of this the President and four members of the Board of Directors acquired, at the instigation of counsel, on syndicate account, 50,000 shares of the common stock. It was the intention of the members of the syndicate to turn over the stock, at cost, to interests favorably inclined to the new company, and thus constitute a voting trust which should control the United States Leather Company. Such a control, friendly to the management, was considered expedient as the outstanding common stock, of little market value, exceeded the issue of preferred stock. The syndicate

acquired the stock during January, February, and March, 1903, before the publication of the revaluation of the bark lands. As the Agreement failed of adoption the syndicate suffered a loss for over a year. It was finally able to liquidate its holdings during October and November, 1904, on the expectation of the consummation of the fourth and last plan of reorganization.

After the failure of this third plan of adjustment in December, 1903, nothing was done further until April, 1904, when Nathan Allen, a large holder of preferred stock, conferred with Vice President Healy of the United States Leather Company regarding the coöperation of Armour and Company, producers of green hides. Allen had already had considerable dealings with Armour & Company. Some months later a meeting was arranged between P. A. Valentine, of Armour & Company, and Vice President Healy. This meeting took place in Chicago in the late summer and with it began the negotiations which ended finally in the reorganization of the United States Leather Company into the Central Leather Company.

From the very beginning the leather combination had been weak in its control over the market in which it bought its hides. It seemed clear that if the Chicago packers could be induced to coöperate in the management of the company, a great and permanent trade advantage would be insured. The Armours had their price. At first they asked $9,000,000 of stock in the reorganized company, but "after serious and protracted discussion the amount of $6,200,000 was finally fixed."[1] This ample allotment to the Chicago packers was not considered a gift. On the contrary it was widely heralded that the Armours would sell their hides to the United States Leather Company on more favorable terms than they extended to other tanners.

[1] It is believed by the writer from information derived from reliable but indirect sources that the amount first proposed by Valentine was ten million instead of nine as stated in the affidavit, and that the final agreement on $6,200,000 — 10 per cent of the outstanding common stock — was due to one of the Armour representatives who had charge of the sale of their hides. It was the plan of the Armour representatives before entering the conference, to begin their negotiations on the basis of a high figure and gradually work down in accordance with the attitude of the Leather Directors. Afterwards they expressed surprise that the leather interests acceded to so high a figure.

The good will and the coöperation of the packers were supposed to have a pecuniary value. Yet the real advantage to the Leather company arising from the coveted coöperation is problematical. The agreement between the Armours and the committee of the Leather company required that the former parties pay for the expenses of the reorganization. Considerable expense was involved in the underwriting, for the Armour interests agreed to acquire sufficient stock in the United States Leather Company to insure the consummation of the plan. Another large expense was a fee of $15,000 to each of the five members of the committee of the management of the Leather company with whom the plan was negotiated. Yet, and here is the weakest point in the whole agreement, the Armours did not agree to sell hides to the United States Leather Company on better terms than those extended to its competitors, nor did the Armours agree to retain their stock. There was absolutely nothing in the agreement to prevent the Armours, once in command of the situation, from administering the Leather company in the interest of their packing business. Should they fail in this, they could sell their stock on the open market and withdraw their coveted coöperation. Before the plan of reorganization was published, while negotiations were in progress with Vice President Healy and others, the Armour interests bought 150,000 shares of the common stock of the United States Leather Company, ostensibly to vote for the resulting plan and thereby insure its acceptance. The common stock was then selling in the neighborhood of $10 a share. In the course of the negotiations the Armour interests stood out clearly in every particular for the interests of the common as against those of the preferred stock, and the reorganization presently to be consummated was of manifest benefit to the common stock, since it would remove the burden of accumulated dividends on the preferred stock. When the plan was made public the price of the common stock rose to $15 and later $21 per share.

The final agreement between the various interests was framed in New York in the early part of December, 1904,[1] and the re-

[1] The definite understanding between the parties was concluded early in November but was not made public until later. This is proved conclusively from the

sulting plan of reorganization bore the date of December 17th. The circular, which announced the plan to the public, gave certain specific reasons for its adoption. Among them were (1) that the working balance originally obtained from the $6,000,000 debenture bonds was insufficient, and (2) that "the establishment of closer relations with interests with which the company necessarily has large dealings and the vesting in them of substantial accounts of the securities of the company, and especially of its common stock, will be a material benefit to the company and to both classes of its stockholders." To accomplish these purposes the committee of the Directors proposed to form a new company that should acquire the physical assets of the United States Leather Company. The securities of the United States Leather Company were to be exchanged for those of the new company on the following basis: For each share of the old preferred stock was to be given 50 per cent of first mortgage 5 per cent bonds, 50 per cent of new 7 per cent cumulative preferred stock and a bonus of 23½ per cent of new common stock. Each share of old common stock was to receive only 30 per cent of new common stock, — each ten shares of old stock being considered equivalent to three shares of new stock. The reorganized company itself had $80,000,000 of stock, divided equally into 7 per cent cumulative preferred stock and common stock. In addition it was proposed to authorize an issue of $45,000,000 of first mortgage bonds. The issue of United States Leather Company's debentures was allowed to remain undisturbed. The distribution of the capital items of the two companies may be seen at a glance from the table given on the next page.

It will be observed that the fixed charges are reduced by an amount equivalent to 2 per cent on the old preferred stock.

Valentine affidavit. On page 143, line 10, Valentine states "neither Mr. Armour nor I was the owner of or in any wise interested in a single share of the stock of said Company, either Common or Preferred, nor did either of us become such owner or so interested until after the general or structural features of the plan of December 17, 1904, had been practically agreed on with Messrs. Hoyt, Healy," etc. Later in the same affidavit (page 145, line 8) this same Valentine states that he and Mr. Armour "purchased, in the open market, during November and December, 1904, . . . 150,000 shares of Common Stock. . . ." *Colgate* v. *Leather Co.*, Valentine affidavit. Also Hoyt affidavit, p. 42.

	UNITED STATES LEATHER COMPANY					CENTRAL LEATHER COMPANY								
							First Mortgage Bonds			Preferred Stock			Common Stock	
	Bonds	Fixed Charges	Preferred Stock	Contingent Charges	Common Stock	Underlying Bonds	Each Stockholder	Aggregate	Fixed Charges	Each Stockholder	Aggregate*	Contingent Charges	Each Old Stockholder	Aggregate
	$	$	$	$	$	$	%	$	$	%	$	$	%	$
Debenture bonds	5,280,000	316,800	—	—	—	5,280,000	—	—	316,800					
Preferred stock	—	—	62,282,300	4,982,584	—	—	50	31,141,150	1,557,057	50	31,141,150	2,179,880	23½	14,636,340
Common stock	—	—	—	—	62,882,300	—	—	—	—	—	—	—	30	18,864,690
To the Armour interests for their coöperation and the expenses of the reorganization		—	—	—	—	—	—	—	—	—	—	—	—	6,200,000
Total issued	5,280,000	316,800	62,282,300	4,982,584	62,882,300	5,280,000	—	31,141,150	1,873,857	—	31,141,150	2,179,880	—	39,701,030
Reserved in treasury to retire debentures, and to acquire other property	—	—	—	—	—	—	—	13,858,850	—	—	8,858,850	—	—	298,970
Total authorized	—	—	—	—	—	—	—	45,000,000	—	—	40,000,000	—	—	40,000,000

Summary	Old	New	Change: Amount	Change: Percentage New to Old
Securities bearing fixed charges	$ 5,280,000	$ 36,421,150	+$31,141,150	690%
Securities bearing fixed and contingent charges	67,562,300	67,562,300	—	100%
Total securities	130,444,600	107,263,330	− 23,181,270	82%
Fixed charges	316,800	1,873,857	+ 1,557,057	502%
Fixed and contingent charges	5,299,384	4,053,737	− 1,245,647	76%

Leaving aside the interest on the outstanding debentures, which remained the same for both corporations, the reorganized company called for the payment of about $1,500,000 on the new bonds and $2,200,000 on the new preferred stock. The total charges were therefore a little over $3,700,000, an amount exactly equal to 6 per cent on the old preferred stock. The average net earnings of the old Leather company, from its inception to the end of December, 1904, had been a little over $3,000,000. The proposal of the reorganization was therefore far from conservative. One of the most important items in any plan of reorganization is the change in capitalization. Is the total capitalization increased or decreased while the actual assets remain unchanged? Counting the underlying debentures as the same in both cases (in round numbers $5,000,000) the capital liability of the old company stood at $130,000,000, that of the new company, including the bonus of common stock to the Armours but excluding the amounts reserved for "additional properties" and "general purposes," at $107,000,000. This, it will be observed, represents a slight reduction in capitalization, and if the $6,000,000 given to the Armours is still further subtracted the reduction is more marked. Considering, however, that the securities bearing charges remain essentially unchanged, and that the common stock, which alone is reduced in amount, was given originally as a bonus, the reduction in capitalization is not as significant as might at first sight appear. Furthermore one should observe that the United States Leather Company was capitalized during the earlier period of industrial promotion, when the issuing of bonds was seldom considered conservative. The new company was burdened by over $30,000,000 of bonds carrying upwards of $1,500,000 in fixed charges, a failure to pay the interest on which might throw the company into bankruptcy. The strength of the old company, in its practical freedom from fixed charges, was sacrificed in order to reduce the contingent charges and obtain new working capital. Viewed in the perspective of conservative finance it is doubtful if the sacrifice was worth while. Yet in the minds of the officers of the company the consummation of the plan of reorganization seemed likely to secure the advantages of a more liberal charter, the coveted coöperation of

a powerful group of packers, the extinction of the claim to unpaid dividends and a subsequent improvement in general credit, the reduction of capital charges, and the acquisition of better facilities for obtaining bank credit.

Before attempting to estimate the inherent justice of the plan, one must consider the question of the status of the timberland surplus of the United States Leather Company. This surplus, it will be remembered, arose from an increased valuation placed upon the company's large hemlock forests. The timber of these forests, but not the bark, had been sold to a subsidiary company and the increased value of the lands was represented partially by bonds of this concern in the treasury of the United States Leather Company. It was argued by the Directors and those who believed that the terms offered the preferred shareholders were just, that this revaluation surplus could not be used rightly for the adjustment of their accumulated dividends. The original contract between the corporation and its preferred shareholders stated that dividends should be paid only out of net earnings. Increase in the value of real property could not be construed as net earnings. Moreover, the revaluation was based on the assumption that the Leather company was a "going concern," a contention which seemed to imply that the new value placed upon the lands was excessive if the property was to be sold in the open market. In opposition to these views those who considered the plan unfair to the holders of the preferred stock pointed out that timber representing the increase in value of the bark lands had been sold and the Leather company had received merchantable securities in payment. These securities were, therefore, net earnings and could be rightfully used to liquidate the claims to unpaid dividends. To reënforce their position they reverted to the circular sent to the stockholders in May, 1903, in which the same Directors declared explicitly that the surplus belonged to the preferred stockholders for the settlement of their dividend claims. The question is certainly an interesting one from the point of view of accountancy. Its solution would seem to depend, in the opinion of the present writer, upon the intent behind the sale of the timber to the subsidiary company. If this transfer actually represented

a *bona fide* sale of property without involving a corresponding diminution of capital assets, then the profits were certainly a part of the net profits of the business and could be used legitimately to reduce the outstanding obligations to the preferred shareholders. If, on the contrary, the formation of a subsidiary corporation involved only a legal fiction and the transfer of lumber to it indicated no *bona fide* sale, then the profits arising were certainly not net profits and could not be used to liquidate the claims of the preferred shareholders. The question, unfortunately, was not passed upon by the court,[1] when the whole reorganization came under its review.

The question of the fairness with which the preferred stockholders were treated is one of particular importance in this reorganization since there adjustment of capital was entirely voluntary on the part of the stockholders. It followed no legal failure nor was it suggested as the solution of financial difficulties which might lead to bankruptcy. It was based on grounds of general expediency alone, and no plan of financial readjustment can be permanently expedient which is not, at the same time, fair to all interests concerned. Setting aside the question of accountancy, as to whether or not the bark land surplus was strictly chargeable to the company's profit and loss account, it would seem that the justice of the reorganization was defensible upon either of two lines of evidence, — the actual value of the property at issue or the market value of the various securities concerned in the reorganization. That is, the fairness of the reorganization can be tested by the equity or inventory value of the assets behind the preferred stock ; or by the market value of the securities before and after the consummation of the reorganization.

When we consider the former of these two questions, we must

[1] Two of the leading cases regarding the legal status of a surplus in excess of a stock liability are *Williams* v. *Western Union Telegraph Co.* (93 N.Y. 162) and *Roberts* v. *Roberts-Wicks Co.* (184 N.Y. 257). In the former Earl, J., states that when the property of a corporation exceeds its capital stock "such surplus, in a strict legal sense, is not a portion of its capital and is always regarded as surplus profits" (p. 188). And in the second case, Gray, J., said "When the property of a corporation has accumulated in excess of its chartered capital, the excess may be regarded and dealt with as constituting a surplus of profits" (p. 266).

remember that at the time the tanneries and bark lands were acquired in 1893 there was little doubt in the minds of the tanners but that they were paid for in preferred stock on the basis of a fair valuation. The $6,000,000 of debenture bonds were issued for money, the bankers taking their commission in common stock. This money was invested directly in the business. We may therefore say, for the purposes of this accounting, that the properties of the Leather company were, on a fair market valuation, originally worth the face value of the preferred stock and the debentures, $68,283,300.[1] On January 1, 1905, a fair date for comparison, the United States Leather Company had acquired a surplus from the net earnings of $3,964,813, and a surplus from the revaluation of the bark lands of $14,235,198, making a total surplus of $18,200,011. The small surplus from net earnings had been largely invested in the properties, so that on January 1, 1905, a fair valuation of the physical properties of the Leather company would be about $86,483,311, and from this subtracting the debentures, — on January 1, 1905, $5,280,000, — it appears that the preferred stock of $62,283,300 was represented by actual physical property to the value of about $8,203,311. The surplus to the preferred shareholders was therefore about $18,920,011. This represented $30.38 a share. The accumulated unpaid dividends amounted then to 41 per cent so that it is quite right to say that the claim for unpaid dividends was worth about seventy-five cents on the dollar. For this $30.38 per share of actual property the preferred shareholders were asked to accept 23½ per cent in new common stock. On the basis of the market quotation of $15 per share for the old common stock this allowance was worth $11.75. In other words, for a legal claim to $41 per share and an actual inventory surplus of $30.38 per share the preferred holders were asked to accept securities the market value of which was $11.75.[2] From such a statement of the case it would seem that the reorganization was unfair to the owners of the preferred stock. And if we,

[1] As a going business. Tangible assets worth at least $60,000,000.

[2] These estimates can be summarized in the following table. They assume that an adequate depreciation charge was made each year. This assumption is borne out by the fact that the company charged its capital account with the bark it consumed;

further, turn to the equity value of this allowance of common stock the story is not very different. The new common stock would have an equity value, if the reasoning suggested in the preceding paragraph is approximately correct, of about $18,920,-011 of actual property. Dividing the equity value by the par value proposed to be issued, we reached the conclusion that each share of the new common stock had a property value back of it of about $48. The preferred stockholders were to receive 23½ per cent of their holding in this common stock in consideration of their claim to unpaid dividends. In property value this 23½ per cent of common stock had an equity back of it of only about $11. From these figures it appears again that the plan of reorganization was unfair to the preferred shareholders.[1]

But there were other considerations than the mere adjustment of inventory values. If we turn to the market prices of the preferred shares as affected by the reorganization, the story presents another side. The rehabilitation of the company's finances was undoubtedly of general advantage to the credit of the cor-

while it maintained and improved its tanneries out of earnings. The bonds were being retired by a small sinking fund.

Equity Value of Preferred Stock Claim

Surplus from net earnings May 1, 1893, to January 1, 1905	$3,964,813	
Surplus — revaluation of bark	14,235,198	
Total surplus, Jan. 1, 1905		$18,200,011
Preferred stock	62,283,300	
Debentures	6,000,000	
Original property investment		68,283,300
Total physical property, Jan. 1, 1905		86,483,311
Debentures outstanding	5,280,000	
Equity to preferred stock	81,203,311	
Surplus to preferred stock		18,920,011
Surplus per share of preferred stock		30.38
Accumulated unpaid dividends		41.08
Percentage of actual property to preferred claim		74%
Market value of the 23½% new stock offered (on basis of $15 for old stock)		$11.75

[1] The computation is based on the following presumptions:

Equity to new common stock (from preceding note)	$18,920,011	
Common stock outstanding against this	39,701,030	
Equity value per share		$48.00
Equity value of 23½% offered		11.28

poration. This fact is clearly shown by the improvement in the market quotations of its securities. During the first six months of the year 1904, before the publication of any plan of reorganization on the lines sketched above, the preferred stock had an average market valuation of $78 a share. During the time the plan was being worked out, the stock rose steadily in value and soon after the plan was made public it was quoted at $106 a share. During the first half of 1905 the market price of the stock averaged $108 a share, and during the last half $115 a share. It is very clear, therefore, in spite of the estimates outlined in the preceding paragraph, based as they were upon inventory value rather than on market quotations, that the reorganization was of manifest pecuniary benefit to the preferred shareholders. Irrespective of any inventory value, the plan would seem to be fair to the preferred stockholders, since the market value of their shares increased by an amount approximately equal to the unpaid claims to dividends. These two lines of reasoning bring into clear contrast the two different points of view about which all estimates of the justice of a voluntary reorganization center. According to a computation based on inventory values the preferred shareholders were unfairly treated; but if the estimate is based on the enhancement of the value of their securities in the open market, because of the supposed advantages of the reorganization, one must presume that they were treated with the utmost liberality. It is a question of the same order as is frequently presented in financial readjustments, one that emphasizes the importance of intangible factors in determining the value of corporate securities.

The plan of reorganization just sketched did not meet with immediate and unqualified approval. Aside from the grumblings of both preferred and common stockholders,—grumblings that always appear no matter how fair any plan may be,—the two points which called for the most general condemnation were the gift of over $6,000,000 of common stock to the Armours and the slight consideration given to the accumulated dividend claim of the preferred shareholders. However, by February 15, 1905, 413,143 shares of the preferred, and 429,997 of the common stock had been deposited with the Central Trust

Company of New York, and on the following day the committee announced that the plan was operative. On April 12, 1905, the Central Leather Company was incorporated under the Corporation Act of New Jersey of 1893, which permitted of a more liberal charter than the old Corporation Act of 1875, under which the United States Leather Company had been incorporated. Soon thereafter, about May 23d, the interim certificates of the Central Trust Company were exchanged for the bonds and stocks of the Central Leather Company in accordance with a plan of exchange outlined in an earlier paragraph.[1]

In the years immediately following the reorganization, the two companies were in a legal sense separate concerns. This separation, however, was little more than a legal fiction. The directors of the United States Leather Company were directors in the new Central Leather Company. The two companies had identical offices and the same places of business. Although at first merely a holding corporation, the Central Leather Company immediately began to acquire and to operate competing tanneries. They obtained the tanneries of L. Beebe and Sons, N. R. Allen's Sons Co., Cover and Drayton, V. A. Wallin and Co., and certain smaller interests. For these additional properties payment was made partly in treasury bonds and stocks and partly by the sale of these same securities. The Central Leather Company represented, therefore, almost from its inception, an interesting example of an operating and a holding company in one. Beginning July 1, 1905, the full dividends were paid on the preferred stock of the Central Leather Company. The few outstanding stockholders of the United States Leather Company apparently had no alternative other than to accede to the terms of exchange still proffered them or to sell their stock in the market to agents of the management who stood ready to buy it at a liberal price. With only a small minority

[1] The number of sales of the United States Leather Company stock diminished to insignificance and those of the Central Leather Company assumed some appearance of speculative activity. A large amount of the floating supply of the old stock was acquired in the interests of the reorganization and by the close of 1906, 575,180 shares of the preferred, or 92 per cent of the total issue, and 614,828 shares of the common stock, or 97 per cent of the total issue, were in the control of the new company. *Colgate* v. *Leather Co.*, Hammond affidavit, "Exhibit A," p. 146.

interest of the United States Leather Company outstanding the management sought to simplify the organization by a merger of the two corporations. On December 18, 1906, official notices were sent to the stockholders of both companies stating that there would be stockholders' meetings of both companies on January 16, 1907. The immediate purpose of these was stated as the "adoption or rejection of a joint agreement, dated December 8, 1906, entered into by the Directors respectively of the United States Leather Company and the Central Leather Company for the merger and consolidation of the two corporations on the terms and conditions of said Agreement set forth and in accordance with the statutes of New Jersey." The Agreement mentioned was merely the Agreement between identical directors and officers of the two companies to merge. It offered the outstanding stockholders of the old United States Leather Company the terms of exchange by which the Central Leather Company had originally acquired the majority of the stock.

In the notice to the stockholders reference was made to the statutes of New Jersey. At the time in question, 1907, these required only a two-thirds vote of the stockholders of two corporations to ratify a merger. Since the Central Leather Company then controlled over 95 per cent of the United States Company's stock the plan had apparently been actually accomplished, except for legal formalities. But the "best laid schemes" of even astute corporation lawyers "gang aft agley." A firm of New York bankers, James B. Colgate and Company, entered into an agreement with a number of the outstanding minority shareholders of the old Leather company to contest the merger in the hope of compelling the company's management to buy the minority interest at a higher price than that accorded the majority of the stock. Accordingly two suits were brought with that object in view on January 12th, just four days before the special meeting at which it was proposed to ratify the agreement of merger. It is beside our present purpose to review the litigation in any detail. We may note in passing, however, the interesting question concerning the powers of stockholders derived from the statutes under which a corporation's charter is granted; do the statute rights of the original shareholders lapse

when they transfer their stock to other persons? This somewhat academic query assumed importance because the corporation laws of New Jersey were changed less than a month after the formation of the United States Leather Company and the rights of stockholders covering the merger of corporations were different according as they were derived from the earlier or the later statute. The courts did not render a final decision on this question.

The subsequent steps of the reorganization can be told briefly. Vice Chancellor Emory, who delivered the opinion of the lower court in the application for an injunction *pendente lite*, overruled most of the contentions of the Colgate complainants. He held, however, that the merger violated the rights of the preferred stockholders of the United States Company in that it required them to accept the securities of the new Central Leather Company in lieu of their claim for unpaid dividends. With this decision in mind, the directors of the two corporations then presented to the stockholders a modified agreement under date of October 10, 1907, permitting the dissenting minority stockholders to retain "any lawful right . . . to receive any dividends accrued and unpaid." The lower court then modified the preliminary injunction to the extent of allowing this agreement to be submitted to the stockholders of the companies for approval. From this decision of the lower court the original complainants, Colgate and others, appealed to the Court of Errors and Appeals. The case was argued in the higher court June 24, 1908, and a decision was rendered by Chancellor Pitney the first of March following. The court expressed itself very forcibly against the merger on the ground of the difference between the charters of the two companies. The original United States Leather Company, organized early in 1893, obtained merely an old-fashioned charter which permitted it to conduct the leather business, but said nothing about running railroads or doing a hundred other things which find their way into modern corporation charters. The lawyers of the Central Leather Company obtained for their clients a typical New Jersey charter based on the Corporation Law of 1893 which permitted the corporation to do anything outside the state of New Jersey that it saw fit to do, — for instance, to operate railroads. The statutes dealing with the merger of

corporations, even those connected with the Corporation Act of 1893, required that the two corporations to be merged should be organized for the purpose of carrying on businesses "of the same or a similar nature."[1] Yet it should be remarked that the old corporation operated railroads, even though nothing to that effect was mentioned in the original charter. It may be inferred that the case was decided merely on technical grounds, and that the important and essential points in the controversy were left undecided.

On the announcement of this decision a stockholders' meeting was called to modify the charter of the Central Leather Company so that the charters of the two companies should more nearly agree. This was done on August 19, 1909. Meanwhile rumors of settlement out of court became current in banking circles. It was pointed out, rightly perhaps, that the general opinion of the higher court, aside from the difference in charters, was unfavorable to the proposed merger. This being so, the leather companies would do well to "settle" with the minority stockholders rather than risk another hearing. On September 23, 1909, the Colgate suit was withdrawn and the terms of settlement were made public a few days later. An offer was made by the Central Leather Company to the minority holders of the old United States Leather Company's stock which embodied an alternative. The stockholders could either accept for each share of old preferred stock $50 in first mortgage bonds, $55 of the Central Leather Company preferred stock taken at 110, and $25 in cash, or else $50 in bonds, $50 in preferred stock, 23½ per cent in common stock, and $10 in cash. This second offer was identical with the original offer in the plan of reorganization with the addition of a *bonus* of $10 a share. On a basis of market values there was little to choose between these two offers and one or other was almost immediately accepted by practically all the remaining stockholders of the United States Leather Company.[1]

[1] The United States Leather Company, as a corporation, is still maintained with a nominal capitalization of $100,000. It is only a selling company. During the comparatively long period of the existence of the old company the name, The United States Leather Company, became widely known among the buyers of leather, and its prestige was high.

Although the contestants, Colgate and others, seemed to be fighting for the rights of a small minority, a large part of those who joined the suit were actuated by no such lofty ideals of abstract justice. Many of them acquired their stock long after the plan of reorganization was made public and some even after the suit had passed through the preliminary stages of trial. These men entered the contest with no purpose of defending rights already existent. They had a speculative interest only. Reduced to its simplest terms they believed they were in a position, by restraining the merger, to compel the management to offer exorbitant terms of settlement. All reorganization proceedings are impeded by the horde of gamblers who stand ready to buy, on a speculative basis, almost any security of doubtful value and then to clamor loudly for the abstract justice of their rights.

It is not difficult to summarize the history and final reorganization of the United States Leather Company. Conceived originally at a most unfortunate time the combination had to face, at the very outset, the most trying period of the last thirty years. It operated in a business where the burden of a long depression and falling prices was particularly heavy. Had the company been heavily capitalized with bonds instead of preferred stock it would have succumbed. But since the capital charges were contingent, they could be postponed. As a result the unpaid dividends began to accumulate during the first year of the company's history and acted as a burden during its entire existence. The company did not suffer from the administration of inferior men. The first president of the United States Leather Company, Mr. Procter, was said to have been the ablest man in the leather business. But it is improbable that there exist men of sufficient business ability to manage a large tanning business producing upwards of $50,000,000 worth of leather a year with the same skill that the man of ordinary endowments could manage a small tannery. During the first few years the company felt no need of additional working capital as is shown by the fact that two fifths of the issue of $10,000,000 of debenture bonds were never sold. But beginning with the trade expansion which set in about 1899 this need began to be felt. So that in

the successful reorganization of the company the provisions for an ampler working capital were quite as important as the relief from the burden of accumulated dividend charges. The reorganization turned on the consent of the preferred stockholders to suffer a reduction in income and the common stockholders a reduction in the par value of their security. As a result both the capital charges and the capitalization were reduced. In these respects the reorganization is typical of most industrial reorganizations and in contrast to most railroad reorganizations. It is its simplicity that makes the history of the United States Leather Company significant for the general study of industrial finance.

XII

UNITED STATES SHIPBUILDING COMPANY[1]

Incorporation

THE United States Shipbuilding Company was incorporated on June 17, 1902, under the laws of the state of New Jersey. The incorporators were Howard K. Wood, Horace S. Gould, and Kenneth K. McLaren. . . . The incorporators collectively subscribed for fifteen shares of the preferred and fifteen shares of the common stock of the company.

On June 24, 1902, the incorporators above named, constituting the stockholders of the company, held their first meeting. . . . At this meeting Frederic K. Seward was elected a director for one year, Raymond Newman was elected a director for two years, and Louis B. Dailey was elected a director for three years, the minutes of the company reciting that Howard K. Wood, one of the incorporators and subscribers to the stock, had assigned his right to one share of common stock to each of the persons above named to qualify them as directors. No stock of the United States Shipbuilding Company, however, was issued to or placed in the name of these directors, so far as the records of the company disclose.

On the said 24th day of June, 1902, the first meeting of the directors of the United States Shipbuilding Company was held. At this meeting there were present Louis B. Dailey, Raymond Newman, and Frederic K. Seward, being all of the directors. The minutes recite that the Board proceeded to the election of officers for the ensuing year, and, ballots having been cast and counted, it was found that Raymond Newman had been elected

[1] From Report of James Smith, Jr., Receiver, filed Oct. 31, 1903; United States Circuit Court, District of New Jersey, *R. R. Conklin, et al.* v. *United States Shipbuilding Co.* [Condensed by omission of immaterial parts and legal repetitions.] For additional references, see p. 438.

president; Louis B. Dailey, vice-president; and Frederic K. Seward, secretary and treasurer. The persons above named as incorporators were . . . all connected with the Corporation Trust Company of New Jersey as officers or otherwise, and the place of residence above stated being the New Jersey office of said Trust Company. The directors were also employees of said company.

At this meeting of the directors an offer was received from one John W. Young, of which the following is a copy:

Offer of Promoters

New York, June 24, 1902

To the Board of Directors, etc.,

I hereby offer to convey, sell, etc., . . . unto your Company for the consideration hereinafter stated, the following property, viz.:

(1) All of the capital stock of the Union Iron Works of San Francisco, Cal., . . . together with all of its property, real and personal, business and good will as a going concern, I hereby agreeing that this corporation has no bonds out and no indebtedness except current accounts, etc.

Messrs. Henry T. Scott and Irving M. Scott have agreed with me . . . to enter into the usual contract with your Company not to compete with it in its business, and not to employ their capital . . . for the period of ten years.

This offer of the stock and property of the Union Iron Works is made also upon the following express conditions, viz.: That your Company shall enter into a contract extending over a period of five years with Messrs. . . . , now connected with the management of the Union Iron Works, to act as officers or managers . . . for this period of five years at an annual salary to be paid to each of $10,000, etc.

(2) The entire capital stock of the Harlan & Hollingsworth Company of Wilmington, Del., etc.

(3) Also the entire capital stock of the Eastern Shipbuilding Company, etc.

(4) All of the real estate of the Canda Manufacturing Company, etc.

(5) Also the entire capital stock of the Crescent Shipyard Company . . . and the business of the Crescent shipyards heretofore conducted by Lewis Nixon.

* * * * * * * *

(6) Also the entire capital stock of the Samuel L. Moore & Sons' Company. . . .

(7) Also the entire capital stock of the Bath Iron Works . . . and of the Hyde Windlass Company. . . .

(8) Also 300,000 shares out of an entire issue of 300,000 shares of the capital stock of the Bethlehem Steel Company . . . engaged in the business of manufacturing and dealing in iron and steel and the products thereof.

I will also pay, or cause to be paid, to your Company $1,500,000 for working capital, and will also deliver, or cause to be paid and delivered to your Treasurer or other nominee, the following securities, viz.: $1,500,000 in par value 5 per cent, thirty-year gold bonds of United States Shipbuilding Company, the same to be held as Treasury assets and disposed of for working capital or other purposes of the Company as your Board of Directors shall hereafter determine.

It is a further condition of this offer that in cases where your Company shall acquire both capital stock and properties of any of the corporations included in this offer, you shall guarantee, or otherwise assume, any promissory notes or other obligations which it may be necessary or desirable to put into the treasuries of such corporation or corporations for the protection of their creditors, or to avoid violation of the statutes of any state or states.

I will accept in full consideration for the conveyances . . . above offered to be made $19,998,500 in par value of the full paid and non-assessable preferred stock of your Company, $24,998,500 in par value of the full paid and non-assessable common stock of your Company, $16,000,000 par value of the first mortgage five per cent sinking fund thirty-year gold bonds, Series A, of your Company secured by a mortgage which will be a first lien upon all the property and plants of the Union Iron Works, etc. (above named companies); also $10,000,000 par value of the 5 per cent twenty-year gold bonds to be made by your Company and to be secured by a mortgage upon the shares of stock of the Bethlehem Steel Company and otherwise, as hereinafter stated.

In case you accept the offer of the stock of the Bethlehem Steel Company the purchase must be made upon the following conditions:

(1) The stock . . . is to be deposited with the New York Security & Trust Company under a mortgage or deed of trust which shall be a first lien upon the stock so acquired, and, subject to the priority of the mortgage to secure said $16,000,000 of bonds, shall be a lien upon the property and plants covered by said $16,000,000 mortgage. . . . The holders of each $1,000 par value of said bonds to have the same voting power as the holders of each $1,000 par value of the stock of your Company.

(2) For the purpose of further securing said issue of $10,000,000 of bonds, your Company shall also procure to be executed and delivered to the New York Security & Trust Company, the single bond of the Bethlehem Steel Company payable to said Trust Company for the sum of $10,000,000 gold coin, with interest thereon at the rate of five per centum . . ., conditioned for the due payment of the principal and interest of said issue of $10,000,000 of bonds, etc.

(3) That an agreement shall be executed between the Bethlehem Steel Company and your Company, by which said agreement your company shall undertake to guarantee so long as any of said issue of $10,000,000 bonds are outstanding, that the Bethlehem Steel Company shall pay dividends upon its capital stock at the rate of Three Dollars per share per year, aggregating an annual dividend contribution of $900,000, and for that purpose that your Company will supply and furnish said Bethlehem Steel Company . . . business and . . . means of earning to enable it to pay said annual dividends . . . or advance sufficient money . . . to make such annual dividend payments which may be credited on any business or work which said Bethlehem Steel Company may thereafter have for or on account of your Company. Said agreement shall further provide that so long as any of said issue of $10,000,000 bonds remain outstanding, said Bethlehem Steel Company shall be protected in keeping on hand and maintaining cash or cash assets of not less than $4,000,000 cash value over and above its current business liabilities (not including its present and projected issue of bonds) as its working capital, no part of which shall at any time be used or applied towards the payments of dividends or for purposes other than the operation and conduct of the business of said Bethlehem Steel Company.

(4) That so long as any of said $10,000,000 bonds are outstanding said Bethlehem Steel Company shall always remain an independent and distinct corporation, and shall not be merged in or consolidated . . . unless . . . requested or consented to by the holders of not less than 75 per cent of said outstanding bonds.

(5) That your Company may at any time pay all of said outstanding bonds as an entirety by depositing a sum equal to the par value . . . with interest . . . to the New York Security & Trust Company as trustee.

I will cause to be delivered to your Company suitable deeds, bills of sale and transfers, etc.

* * * * * * * *

(Signed) JOHN W. YOUNG

Upon the receipt of this offer the directors above named, holding no stock whatever in the Company, but at most a mere subscriptive right, by assignment, to one share each, adopted the following resolution:

ACCEPTANCE BY COMPANY

Whereas, John W. Young has offered to convey, sell, etc., . . .; and,

Whereas, In the judgment of this Board the value of the properties so offered . . . is at least the par value of the stocks and bonds of this Company proposed to be issued therefor, to wit, the sum of $70,997,000, and said properties are necessary for the business of this Company;

Resolved, That said offer be and the same is hereby accepted, etc., . . .

Further resolved, That for the purpose of enabling this Company to accept the foregoing offer, it shall as soon as practicable take the steps required by law for the increase of its authorized capital stock from thirty shares of $100 each . . . to four hundred and fifty thousand shares of $100 each, two hundred thousand shares of which shall be preferred stock, and two hundred and fifty thousand shares of which shall be common stock, making a total authorized capital stock of $45,000,000. . . .

Further resolved, That the officers of this Company be, and they hereby are authorized and directed to make . . . to the Mercantile Trust Company as Trustee, a mortgage or deed of trust upon the properties purchased pursuant to the offer of said John W. Young (exclusive of the shares of stock of the Bethlehem Steel Company), to secure the payment of $16,000,000 par value of first mortgage 5 per cent thirty-year sinking fund gold bonds, etc., . . .

Further resolved, That the proper officers of this Company be and they hereby are authorized and directed to make . . . a mortgage or deed of trust to the New York Security & Trust Company as Trustee, of the shares of the capital stock of the Bethlehem Steel Company . . . to secure the payment of $10,000,000 par value of the 5 per cent twenty-year gold bonds of this Company, which mortgage shall contain the provisions required under the terms of said offer, etc., . . .

Further resolved, That the officers of this Company are hereby authorized to execute, issue, and deliver to the said Young . . . the first mortgage . . . gold bonds of this Company of the aggregate par value of $16,000,000, . . . $10,000,000 and certificates for 199,985 shares of the preferred capital stock . . . and for 249,985 shares of the common capital stock, etc.

Increase of Capital Stock

On the same day, to wit, the twenty-fourth day of June, . . . a meeting of the stockholders of said Company was held for the purpose of authorizing and increasing the capital stock of the United States Shipbuilding Company and of considering and acting upon the offer of said John W. Young. There were present Frederic K. Seward, Louis B. Dailey, Kenneth K. McLaren, Horace S. Gould, Howard K. Wood, and Raymond Newman, claiming to be holders of fifteen shares of preferred and fifteen shares of common stock of the United States Shipbuilding Company, being all the capital stock of said Company. At this meeting the following resolution was adopted:

Resolved, That the action of the Board of Directors . . . be . . . approved, ratified, and confirmed, etc.

At a meeting of the Board of Directors of the United States Shipbuilding Company held on July 31, 1902, the following resolution was adopted:

The Board of Directors, etc., do hereby resolve and declare that it is advisable that the capital stock of this Company be changed from thirty shares . . . to four hundred and fifty thousand shares . . . of capital stock, etc.

* * * * * * * *

Purchase of Subsidiary Plants

Between the fifth day of August, 1902, and the twelfth day of August, 1902, in evident compliance with the offer of said John W. Young and the acceptance thereof . . . the companies . . . conveyed to the United States Shipbuilding Company all their real and personal property. . . .

* * * * * * * *

Leases to Subsidiary Companies

Your Receiver further reports that after the delivery of said deeds . . . leases were entered into between the United States Shipbuilding Company and the (various companies hereinbefore named). . . . By the terms of these leases "all the yards, docks, and plant," etc., were leased to the above named constituent companies "at the yearly rent or sum of the net profits of the said party of the second part in its business during the term of this lease." . . . In the Union Iron Works lease the entire plant and property were leased for one year to the Union Iron Works for the nominal rental of one dollar. All such leases were terminable on five days' notice.

Alleged Basis of Directors' Actions

The resolution of the Board of Directors of the United States Shipbuilding Company accepting the offer of John W. Young, above set forth, was stated by said Board in its minutes to be based upon a report in writing from Messrs. W. T. Simpson, Fellow Institute Accounts, New York, and Riddell and Common, Chartered Accountants, on the condition of the business of the several companies mentioned in said offer, excepting the Bethlehem Steel Company. This report is alleged to have certified, among other things, that the contracts of the constituent companies for construction then in hand amounted to over thirty-six millions of dollars. That the time necessary to complete the work contracted for averaged about eighteen months from January first, nineteen hundred and two, and that the estimated net profits thereon had been calculated at over five millions of dollars. That new work was being constantly offered, and this new work, replacing completed contracts from time to time, should result in the realization of an average annual profit on work in hand and in sight of two million two hundred and twenty-five thousand dollars.

With reference to the Bethlehem Steel Company, the minutes of the Board of Directors recite that Messrs. Jones, Cæsar & Company, chartered accountants, had been investigating the affairs of the Bethlehem Steel Company, and had made a report

that the company was earning at the rate of one million eight hundred thousand dollars per year; that it had a working capital of over four millions of dollars, and that it had contracts in hand sufficient for its full running capacity for three years. In réliance upon these alleged reports, and without knowledge of, or investigation into, the merits of the properties, the resolution in question was adopted.

Acts of the Directors

A comparison of the figures alleged to have been relied upon by the Board of Directors in accepting the offer of John W. Young, with the true figures ascertained from an examination of the subsidiary companies subsequent to the purchase of said plants, discloses so great a variance as to impel the belief that the figures contained in the minutes were wilfully misstated. It is extremely doubtful whether any report was submitted by any accountants made as of that time, as the minutes recite. In a certain Prospectus marked "Private and Confidential," bearing date the 19th day of April, 1902, there is contained a letter purporting to be signed by Messrs. Simpson and Riddell and Common, under date of January 24th, 1902, which letter would seem to serve as a basis to a certain extent for the allegation in the minutes of the Board of Directors. If the examination of these accountants was made as of January 1st, 1902, as the letter would imply, it must have been of the most superficial kind. The letter in question makes such exaggerated representations with reference to the profits, present and prospective, as to make it absolutely worthless as a guide in ascertaining the real condition of the plants. It is entirely refuted by their later reports and detailed statements made as of June 30th and July 31st, 1902.

Your Receiver has seen and inspected the statements made by these accountants as of June thirtieth, nineteen hundred and two, and July thirty-first, nineteen hundred and two, and finds nothing therein to support the statements contained in the minutes of the Board of Directors.

The statement of Messrs. Simpson and Riddell and Common of the condition of the subsidiary plants as of June thirtieth, nineteen hundred and two, contains, among other things, the following figures:

1. Contract price	$34,377,408.70
2. Value of work done under said contracts up to June 30, 1902 .	13,771,768.96
3. Value of work to be done under said contracts subsequent to June 30, 1902	$20,605,639.74

The report of these accountants also contained a statement of the volume of business done by the constituent companies for the three years ending June thirtieth, nineteen hundred and two, on which the profit was shown to be about ten per cent. The report also shows that the contracts remaining unfinished on June thirtieth, nineteen hundred and two, would require three years for their completion.

From this report the following facts clearly appear:

1. That the amount of contracts on hand June thirtieth, nineteen hundred and two, instead of being Thirty-six Millions of Dollars, as recited in the minutes of the Board of Directors, was $15,394,360.26 less than the amount therein stated.

2. That it would take three years to earn whatever profit was involved in these contracts, instead of eighteen months, as alleged in the minutes.

3. That the profits on such contracts, instead of amounting to $5,000,000, as the minutes recite, basing the estimate upon the past earnings contained in the report, would be about two millions of dollars; and,

4. That the statement that the average annual profit on work in hand and in sight of the constituent companies, exclusive of the Bethlehem Steel Company, was $2,225,000, appears to have no more substantial basis than the wildest conjecture.

AMOUNT OF CONTRACTS, JULY 31, 1902

Your Receiver has caused to be prepared a statement showing the contracts in force on the 31st day of July, 1902, the portion thereof completed, the balance remaining uncompleted, and the estimated profit thereon, based upon the highest possible estimate of earnings, which is annexed hereto marked "Schedule No. 2," and made a part thereof. From this statement it appears that the face value of the contracts on hand, including extras, on July 31, 1902, was	$34,097,739.23
The value of work done on said contracts up to July 31, 1902, was .	14,295,195.15
Leaving the value of the uncompleted work on said contracts on July 31, 1902	$19,802,544.08

Estimated Earnings on Such Contracts

Adopting the figures of the accountants and estimating profit on the basis of percentage of completion reported by them and the actual cost of such percentage, the highest possible estimate of earnings on the balance of the contracts to be completed would be $2,203,269.83, as appears from said "Schedule No. 2."

An examination of the books of the Company, however, with care and the exercise of some intelligence, and adjusting the amount of the contracts at corrected figures, would have shown that there was no basis for the foregoing figures, but that there might be justification for an estimated profit of $1,660,021.59, as appears from the statement hereto annexed, made a part hereof and marked "Schedule No. 3."

An examination as of August 1, 1903, however, with the past year's work as a basis, and allowing for changes in extras, discloses another set of figures and shows that the profit on such uncompleted contracts cannot exceed the sum of $1,078,261.42, as appears from the statement hereto annexed, made a part hereof and marked "Schedule No. 4."

From this latter Schedule, which is based upon the actual cost of the work, so far as ascertainable, a situation is disclosed so much at variance with the figures alleged to have been relied upon by the Board of Directors as to lead to the belief that the minutes of the Board of Directors in this respect must have been wilfully falsified. The Five Millions of profits dwindle to about One Million; the contracts therein referred to will not be completed for upwards of three years, and, judging from past experiences, it is safe to say that this estimated profit will suffer great depreciation before the completion of the contracts.

Working Capacity of Plants in Relation to Earnings

So far as your Receiver is able to ascertain, the full capacity of the yards, exclusive of the Bethlehem Steel Company, is about fourteen million dollars of work annually, while twelve million dollars is an average volume of work. From the figures contained in the report of the Messrs. Simpson and Riddell and

Common, it appears that the average profit of the yards for the three years preceding their purchase by the United States Shipbuilding Company did not exceed ten per cent. Upon this basis the average annual profit derived from the yards, on the basis of the capacity above stated, would not exceed a million four hundred thousand dollars.

Earnings for the Year ending August 1, 1903

This basis, however, is no guide to the actual earnings of the constituent companies. After being in operation for one year under the control of the United States Shipbuilding Company, the earnings of the constituent companies, exclusive of the Bethlehem Steel Company, instead of being $2,225,000, as alleged by the Directors, or $1,400,000, as figured on the above basis of ten per cent, did not exceed $833,458.74, as appears from "Schedule 5," hereto annexed and made a part hereof.

It has been suggested that the poor showing in regard to earnings is due to the increased cost of labor and material during the past year. It is true that the cost of labor was greater during the past year than the previous years, and that there were some losses occasioned by strikes; but it is also true that, by reason of the combination of all the yards under one management and the attempted control thereof by the United States Shipbuilding Company, there should have been a great reduction in the management expenses. This reduction in expense, however, did not come to pass, and one reason for it may be found upon an examination of the offer of Young, above set forth. In this offer it will be found that in the case of the Union Iron Works, Eastern Shipbuilding Company, Samuel L. Moore & Sons' Company, Bath Iron Works, and the Hyde Windlass Company, it was provided that the United States Shipbuilding Company should enter into contracts with certain persons therein named for upwards of five years at salaries, in many instances, greater than the earnings of the subsidiary company would warrant. The acceptance of this offer, therefore, with these conditions imposed, not only reduced the earnings of the subsidiary companies, but left the officers in charge

thereof practically free from interference by the Board of Directors of the United States Shipbuilding Company for a period of five years, a fact that must necessarily have had considerable influence upon the management and earnings of the individual plants. This fact, however, does not wholly explain the failure of the earnings of the constituent companies to reach the amount of earnings estimated in the preliminary reports. The real reason why the earnings fell below the anticipated profits was because previous alleged earnings had been figured upon a percentage of completion of contracts, which percentage in many instances was erroneous. For instance, in the case of the torpedo boats "Nicholson" and "O'Brien," it was stated that these boats were fully completed. As a matter of fact there was subsequently expended thereon the sum of $56,271.04, and it is estimated that upwards of $20,000 is still needed to complete these boats. Your Receiver, therefore, respectfully submits that the method of arriving at profits earned previous to the combination was practically worthless for the purpose of ascertaining accurate results, and led to the inaccuracies in the estimates for the future.

Bethlehem Steel Company

In regard to the Bethlehem Steel Company, the minutes of the Board of Directors with reference to the offer of the said Young, recite that an investigation of the affairs of that company discloses that it was earning at the rate of $1,800,000 a year, and that it had a working capital of over $4,000,000. For the two years preceding the adoption of the resolution in question by the directors the earnings of the Bethlehem Steel Company for the fiscal year ending the thirtieth day of April were as follows:

1900–1901	$381,403.83
1901–1902	978,743.81

From these figures, as to the earnings of the Bethlehem Steel Company, which are made up from the report submitted by the Bethlehem Steel Company, it appears that the earnings of that company at the time of the adoption of the resolution were much below the amount alleged in the minutes of the Board of

Directors of the United States Shipbuilding Company, and that there was then no justification for the use of such figures.

It also appears that the working capital of the Bethlehem Steel Company at the close of their fiscal year on the thirtieth day of April, nineteen hundred and two, was not over $4,000,000, but was at least $250,000 less than such amount, as hereinafter set forth.

Working Capital

From the report of Messrs. Simpson and Riddell and Common, as of July 31st, 1902, not made, however, until after the properties had been acquired and paid for, it appears that the working capital of the constituent companies, exclusive of the Bethlehem Steel Company, was $3,278,798.48. The figures making up this total were subsequently found to be excessive in the case of nearly every company, the shrinkage amounting to $1,450,367.41, so that the working capital of the constituent companies was but $1,828,431.07, as appears from the statement hereto annexed, marked "Schedule No. 6," and made a part hereof. From the statement hereto annexed, marked "Schedule No. 7," and made a part hereof, it appears that with the exception of the Union Iron Works, the subsidiary companies, taken together, had absolutely no working capital; but on the contrary their liabilities exceeded their resources in the sum of $294,719.33. By reference to this schedule it appears that the following was the condition of said companies at the time of their purchase:

DEFICIT		
Bath Iron Works	$3,518.74	
Crescent Shipyard Company	403,192.28	
Harlan & Hollingsworth Co.	73,813.44	
S. L. Moore & Sons' Company	5,039.27	
		$485,563.73
SURPLUS		
Eastern Shipbuilding Company	$1,391.34	
Hyde Windlass Company	189,453.06	
		$190,844.40
Net Deficit being excess of Liabilities over Assets		$294,719.33

From an examination of "Schedules 6 and 7," it will appear that the alleged working capital was provided largely by the

Union Iron Works, with slight help from the Hyde Windlass Company and the Eastern Shipbuilding Company.

The amount of Accounts Payable and Notes Payable of the different companies at the time of their purchase by the United States Shipbuilding Company was $2,334,987.64. Of this amount $2,192,145.98 was owing by the subsidiary shipbuilding companies other than the Union Iron Works, as appears from said "Schedule No. 7." As the principal part of the alleged working capital above mentioned was confined to Union Iron Works, it will appear that so far as the remaining companies are concerned, when taken over by the United States Shipbuilding Company, they not only had no working capital, taken collectively, but were in immediate need of financial assistance.

From the foregoing facts, viewed not only in the light of subsequent developments, but also from the figures obtainable at the time of the incorporation of the United States Shipbuilding Company, it appears to have been the intention of those responsible for the statements and figures alleged to have been relied upon to mislead and deceive the investing public and the then present and future creditors of the Company.

Prospectus

In this connection, your Receiver begs to refer to the prospectus issued to the public, with a view to inducing subscriptions for the bonds of the United States Shipbuilding Company, under date of June 14, 1902. This prospectus seeks to invite the public to subscribe for nine millions of dollars of the first mortgage 5 per cent sinking fund gold bonds of the United States Shipbuilding Company. It recites that the United States Shipbuilding Company "has been organized under the laws of the State of New Jersey." It implies that the total capital stock of the Company is twenty millions of dollars, $10,000,000 of which is preferred and $10,000,000 common. It sets out a list of the directors of the United States Shipbuilding Company, numbering ten in all. It recites that the subsidiary plants of the Company, exclusive of the Bethlehem Steel Company, have been appraised as going concerns at twenty millions of dollars ; that

these companies would have a combined working capital of more than five million of dollars; that they have on hand contracts for work amounting to more than $36,000,000, on which the profits were estimated at over $5,000,000.

Waiving for the present all discussion as to the value of the plants as going concerns, a comparison of this prospectus with the facts disclose the following false and misleading statements:

1. At the date of this prospectus the United States Shipbuilding Company had not been incorporated.

2. Its capital stock was never Twenty Millions. Originally it was Three Thousand Dollars; which amount was subsequently increased to Forty-five Millions.

3. Six of the ten persons mentioned as directors in the prospectus were not directors of the company, and never have been.

4. The amount of contracts on hand did not exceed $36,000,000, their face value being $34,182,861.94, but of this amount a profit was available only on the uncompleted portion of the contracts, which profit, as heretofore shown, will not exceed $1,078,261.42, and will take three years to earn.

5. These companies did not have a working capital of more than $5,000,000; the figures of the accountants show only a working capital of $3,278,798.48. This working capital, however, was almost obliterated by subsequent adjustment, as hereinbefore set forth.

6. The statement that the profits on contract work in hand would be $5,000,000 was undeniably false. If it is claimed that the profit was estimated on the entire amount of $36,000,000, the answer to this is that, admitting there was $36,000,000 worth of contracts (which was not true), the utmost profit that could be looked for, according to the figures of the accountants, was $3,600,000. When this prospectus was issued, the persons who were responsible for it must have deliberately disregarded figures which would have shown that the amount of work still to be done on the contracts was but $20,605,639.74, instead of $36,000,000, and that upon such uncompleted work a liberal estimate would have placed the earnings at only a trifle over $2,000,000.

VALUE OF THE PLANTS

The net surplus of the various constituent companies, including their plants, according to the statement of the accountants, as shown by the books of said companies, were on the 31st day of July, 1902, as follows:

Bath Iron Works	$827,316.19	
Hyde Windlass Co.	358,121.29	
Crescent Shipyard Co.	470,583.99	
Samuel L. Moore & Sons' Co.	404,788.88	
Eastern Shipbuilding Co.	237,278.53	
Harlan & Hollingsworth Co.	1,294,767.16	
Union Iron Works	4,303,378.97	
Total	$7,896,235.01	
Bethlehem Steel Co. (deducting underlying mortgages)	4,245,281.25	
Canda Manufacturing Co. (estimated)	300,000.00	
Total		$12,441,516.26

For this property the directors of the United States Shipbuilding Company parted with the following obligations of that company:

Preferred stock of the U. S. S. Co.	$19,998,500	
Common stock of the U. S. S. Co.	24,998,500	
First mortgage 5 per cent bonds	16,000,000	
Twenty-year gold bonds	10,000,000	
Total		$70,997,000.00

There was returned to the company, however, the following cash and securities:

Cash	$1,500,000	
First mortgage bonds	1,500,000	
Total		$3,000,000.00
Total bonds and stock paid by Shipbuilding company's directors for the subsidiary plants		$67,997,000.00

In connection with the purchase of the Canda Manufacturing Company, $1,100,000 of the cash and securities of the United States Shipbuilding Company were parted with. The Canda company gave up nothing except its lands and buildings, its good will, if any, and practically all of its machinery being retained by the vendors. The above estimated value of $300,000 is undoubtedly greatly in excess of its true value. No use has

ever been made of this plant, and none was apparently contemplated when it was purchased. After its purchase the directors of the United States Shipbuilding Company caused an inquiry to be made with a view to ascertaining whether it could be put to any use, and an adverse report was made. (See minutes of the directors.) Why this property was purchased at all is not apparent.

Viewing the acquisition of the properties from the standpoint of the surplus and plant values, as disclosed by the books of the companies, the directors appear to have made a gift of upwards of $55,000,000 worth of stock and bonds of the United States Shipbuilding Company entrusted to their care.

It may be claimed, however, that the book values give no adequate idea of the real value of the plants as going concerns, and that the earnings of the plants should be taken into account in ascertaining such value. With reference to this matter, the minutes of the directors recite that the constituent companies, exclusive of the Bethlehem Steel Company, had an earning capacity annually of	$2,225,000.00
and that the Bethlehem Steel Company was earning . . .	1,800,000.00
Making a total earning capacity of	$4,025,000.00

This statement was false, and must have been known to be so at the time the plants above mentioned were taken over. It can serve no useful purpose, therefore, in establishing value from the standpoint of earning capacity. In this connection the earnings of the past year are presented for consideration:

The earnings of all the companies for the year ending July 31st, 1903, were as follows:

Constituent companies	$833,458.74
Bethlehem Steel Company (net earnings) after deducting interest on underlying mortgages, discounts, and depreciation . . .	1,662,530.80
Total	$2,495,989.54

A word of explanation with reference to the earnings of the subsidiary shipbuilding companies. These earnings, as to continuing contracts, are arrived at as follows: An estimate is made of the proportion of the contract completed. If this proportion should represent 50 per cent of the entire contract, and the actual cost of such percentage should be found to be 10 per cent less than the proportion of the entire contract price then earned, the profit, when such estimate is made, is put down at a figure which

will represent 10 per cent of such earned proportion of the contract price. Frequently this method of arriving at profits is found to be erroneous. The percentage of completion is found to have been placed too high, and as a consequence, the profits on the entire contract are reduced much below the estimate, and, in many cases, entirely wiped out and a loss sustained.

With reference to the Bethlehem Steel Company, a different method prevails. The method of the latter company is to take profits only upon deliveries, and not to estimate earnings as the work progresses. By this method the actual profits may be arrived at.

Assuming, however, that the earnings of the constituent companies are correctly set forth above (and in the case of Bethlehem they are not understated), of what use are such earnings for the purpose of establishing values unless they are available by the United States Shipbuilding Company?

These companies claim to have earned $2,495,989.54, but the United States Shipbuilding Company has been benefited to the extent only of a trifle over twelve per cent of this amount. Of these alleged earnings the constituent companies have paid during the eleven months ending July 1, 1903, to the United States Shipbuilding Company	$60,754.23
The Bethlehem Steel Company, for the purpose of meeting the semi-annual interest on the $10,000,000 mortgage . . .	250,000.00
Making a total of	$310,754.23

Of the $833,458.74 alleged to have been earned by the Shipbuilding companies, there has been expended for new machinery . .	$165,066.38
Of the earnings of Bethlehem company there was expended for plant betterment	683,370.24
There was paid by all of the companies to the United States Shipbuilding Company, as above stated	310,754.23
Making a total of	$1,159,190.85

The balance of the earnings (considering the above amount as having been earned) amounting to the sum of $1,336,798.69, was retained by the companies. By reason of the unsafe method of ascertaining the profits of the shipbuilding companies, it is extremely doubtful whether they have earned any such amount as above set forth. It is true, however, assuming that their earnings have been as above mentioned, that their financial condition has not been such as to warrant them in withdrawing any consider-

able sum from their assets for payment to the United States Shipbuilding Company. The utmost that they could do during the past year was a trifle over seven per cent of the amount claimed by them to have been earned. The Bethlehem company, during the past year, insisted that no sum in excess of the $250,000 paid by them to meet the interest on the $10,000,000 instrument, known as the Schwab mortgage, could be withdrawn from their assets for payment to the United States Shipbuilding Company; or, in other words, that about fifteen per cent of their entire earnings was the best they could do for the United States Shipbuilding Company. Concerning the earnings of the Bethlehem, your Receiver will deal at length elsewhere in this report, but it may be said here that Bethlehem deliberately used up its earnings in making enormous purchases of material for its own benefit, and in extensions, improvements, and repairs, in order apparently to keep its earnings from the United States Shipbuilding Company.

On the basis of what the United States Shipbuilding Company received from all the companies last year, there would be sufficient income only to meet the interest, at five per cent, on an investment of a trifle over $6,000,000. It may be insisted that this is not the best the companies can do, and therefore this amount should not be taken as a guide in establishing the value of the plants. Your Receiver is satisfied that it is not the best the companies can do, especially in the case of Bethlehem. It is certain that better returns would have been received from the constituent companies if they had been brought within closer reach of the central company, and if officers had been placed in charge who had looked to the interests of the central organization and not wholly to the betterment of the constituent companies. It is undoubtedly true that the fastening upon the constituent companies of certain officials, at fixed salaries, and for a long term of years, practically beyond the reach of the central organization, has materially prevented the United States Shipbuilding Company from obtaining the best results from its properties. In the case of the Bethlehem, a Board of Directors having the welfare of the United States Shipbuilding Company at heart, rather than its destruction, would have conduced much to the gain of the latter company. With these defects in man-

agement removed, the earning capacity of all the companies, so far as the United States Shipbuilding Company is concerned, would be greatly enhanced.

At the end of eleven months of operation, the United States Shipbuilding Company was adjudged insolvent and a receiver appointed. This was due either to the fact that the earnings were insufficient to meet its obligations, or because those earnings were improperly diverted. Your Receiver will hereinafter discuss this matter, but under this head he respectfully submits that the earnings of the several companies during the past year may not safely be used for the purpose of establishing the value of the plants.

Excessive Price paid for Plants

Considering the value of the plants, therefore, either from the standpoint of the books, or the earning capacity of the companies, and allowing for an increase in earnings in the future, it is evident that the accommodating directors of the United States Shipbuilding Company, in acquiring these properties, deliberately gave away many million dollars in the stock and bonds of their Company.

Who participated in this wholesale plunder? The testimony now being taken in the above entitled proceedings will doubtless disclose the name of all the participants; but as such testimony will be submitted to this Court for action, your Receiver does not deem it proper to comment upon it here. Certain it is that much of this vast amount of stock and bonds was taken by persons and corporations who parted with little or no consideration in exchange therefor. Blocks of the stock went to the vendors of the constituent plants and to the purchasers of bonds, as bonus, absolutely without benefit to the Company; $20,000,000 of it admittedly went to Mr. Charles M. Schwab in addition to the agreed price for Bethlehem. Some of it went to the promoters of this artistic swindle; and when all had been provided for, what was left of the bonds, amounting to $1,500,000, was handed back to the Company ostensibly to supply it with "working capital."

From the foregoing statement as to values, it is apparent that the $24,500,000 of bonds given up by the directors was an excessive price for all the plants purchased. Your Receiver is advised that as to the $44,997,000 of the preferred and common stock handed over by the directors to the vendors and promoters of this scheme, it cannot successfully be maintained that any value was paid therefor. Treating the issue of bonds, therefore, as full payment for the properties (and in so doing the Shipbuilding company alone is being injured), it follows that the vendors and promoters and their associates in the transfer and conveyance of the various plants to the United States Shipbuilding Company, by the acceptance of this $44,997,000 of the capital stock of the Shipbuilding company, without paying value therefor, became liable thereon to said corporation, by virtue of the provisions of section 21 of an act of the Legislature of the State of New Jersey, entitled an act concerning corporations (Revision of 1896). The United States Shipbuilding Company was entitled to recover such indebtedness from the holders of such stock and your Receiver is advised that he is entitled to enforce the same. Accordingly, your Receiver has offset against the sum alleged to be due on the $10,000,000 mortgage to the New York Security and Trust Company as trustee, to protect the issue of bonds to Charles M. Schwab, the liability of the said Charles M. Schwab on the $20,000,000 of stock received by him as aforesaid, and has interposed an answer in the suit by said trustee to foreclose the mortgage given as security for said bonds, claiming that by virtue of said offset the total issue of said bonds has been fully paid and satisfied. As to the issue of the bonds under the mortgage for $16,000,000 made to the Mercantile Trust Company, your Receiver charges that many of said bonds were received by the vendors and promoters and their transferees, and were issued by said Mercantile Trust Company, with full knowledge of the right of the United States Shipbuilding Company to be paid for the common and preferred stock taken by said vendors and other holders of said bonds without value, and as to all bonds secured by said mortgage so received, your Receiver has offset against the amount alleged to be due thereon, the liability of the holders thereof on the com-

mon and preferred stock so received by them, or their transferrers, and has interposed an answer in the suit instituted by the Mercantile Trust Company to foreclose said mortgage, claiming that by virtue of such offset the total issue of said bonds, or the principal part thereof, has been fully paid and satisfied.

Culpability of the United States Shipbuilding Company's Directors and Others

Your Receiver has spoken of the directors of the United States Shipbuilding Company as if they were wholly responsible for parting with many million dollars in the stocks and bonds of the United States Shipbuilding Company without value. The directors who were guilty of this act are responsible and should be held accountable for their unlawful act; but they are not alone responsible. In the first place, they were not bona-fide holders of the stock of the United States Shipbuilding Company. They were clerks selected by the promoters of this scheme from the Corporation Trust Company. They took an assignment of a subscriptive right to a share of stock, and upon the strength of this alleged subscription they dealt with the property of the United States Shipbuilding Company in the manner above recited. These young men were mere figureheads, placed in this position in order that the scheme of others might be carried into effect. This scheme was placed before them by its instigators, through the medium of an alleged offer of John W. Young, and the so-called directors in conformity with their instructions, and, without the ability or the knowledge to pass upon the matters therein contained, proceeded to do as they were told. Your Receiver charges that the properties of the various constituent companies were sold to the United States Shipbuilding Company for an amount which the vendors of such properties, at the time of such sale, knew to be far in excess of the fair value of said plants; and that the plan to combine such properties was conceived by certain promoters and was consummated by them with full knowledge of its injustice to the United States Shipbuilding Company.

Your Receiver begs to direct the attention of the Court to the

fact that in the purchase of the various constituent companies, the United States Shipbuilding Company was absolutely without independent and intelligent representation. No inspection of the properties was made on behalf of the Shipbuilding company. No independent appraisement was had. No steps seem to have been taken by any one with a view to protecting the interests of the United States Shipbuilding Company. The directors who purported to act for the Company were the tools of the promoters; the debts of the constituent companies, aggregating $2,334,987.64, seem to have been purposely withheld, and the bonds and stock of the United States Shipbuilding Company were placed wholly at the mercy of the vendors and promoters.

Operation of the United States Shipbuilding Company

Under such auspices the United States Shipbuilding Company began operations. On paper the constituent companies had a working capital in excess of $3,000,000, yet offices had hardly been secured by the United States Shipbuilding Company before the latter company was compelled to assist the constituent companies to pay their debts. The alleged working capital of the constituent companies existed on paper only. It was made to appear as available capital in order that the sale might be consummated. After such sale there was no longer any necessity for the continuance of this pretence, and accordingly demands for remittances began to pour into the central organization. During the eleven months ending July 1, 1903, the United States Shipbuilding Company was compelled to advance to the constituent companies the sum of $1,019,955.78. Of this amount $60,754.23 was returned to the Company, making the net amount advanced to the constituent companies $959,201.55. In addition to this sum it was compelled to part with $520,000 of the bonds which had been placed with it as working capital, for the purpose of securing indorsements on promissory notes which the United States Shipbuilding Company was required to make for the accommodation of the constituent companies.

The reason for this has been herein elsewhere suggested. When the various properties were purchased, the debts of such

companies were not disclosed. Had there been independent, intelligent representation on the part of the United States Shipbuilding Company in connection with the acquisition of these properties, it would have been discovered that the new company was taking over $2,334,987.64 of debts, a considerable part of which called for immediate attention. Had there been such representation, it would have been disclosed that the companies had practically no working capital except such as they might receive from their vendee, and with this knowledge the wholesale delivery of bonds and stocks of the United States Shipbuilding Company would undoubtedly have been averted. But there was no one in that transaction to protect the interest of the new company, and as a consequence it was not only made to pay excessive prices for the property purchased, but obligations were assumed by reason of this vast amount of debt that practically exhausted the resources of its treasury.

While the bills of sale from the various constituent companies purported to transfer all the personal property of such companies to the United States Shipbuilding Company, including their cash, amounting to the sum of $389,317.57 (exclusive of Bethlehem), this amount was retained by the various companies when the leases above mentioned were made, and no benefit therefrom was ever received by the United States Shipbuilding Company, except the doubtful one of allowing this amount to help swell the alleged working capital of the constituent companies.

The United States Shipbuilding Company was not fairly organized until some time in September, 1902. On the 24th day of December, 1902, with a view to inducing the New York Stock Exchange to list the entire stock and bond issue of the Company, amounting to $69,500,000, a statement was made to such exchange, over the signature of A. C. Gary, treasurer of the United States Shipbuilding Company. This statement recites that the earnings of the subsidiary companies, exclusive of the Bethlehem Steel Company, for the year ending June 30, 1902, amounted to the sum of $1,942,522.03, and that the net earnings of the Bethlehem Steel Company for twelve months ending July 31, 1902, amounted to the sum of $1,441,208.03.

Without taking time to controvert this statement, which was clearly erroneous, and which, upon a proper examination, would have been shown to be so, an allegation appears in this statement of far more serious import. It is therein alleged that the net earnings of the United States Shipbuilding Company and the Bethlehem Steel Company for the three months ending November 30, 1902, amounted to the sum of $1,163,022.22. Of this amount the United States Shipbuilding Company was said to have earned up to that time $554,021.45, and the portion earned by the Bethlehem Steel Company was placed at $609,000.77. These earnings were said to be net; but in the case of the Bethlehem Steel Company no allowance was made therein for depreciation, and, furthermore, such earnings constituted no basis for averaging the annual profit, as the later report of the Bethlehem Steel Company shows. In the case of the United States Shipbuilding Company, the earnings existed on paper only, as appears from subsequent reports. Your Receiver believes that the officials of the United States Shipbuilding Company did not know that erroneous reports were being made to them by the constituent companies, but their action was at least injudicious in so wording the statement to the Stock Exchange as to impel the inference that the earnings of the United States Shipbuilding Company up to the 30th day of November, 1902, were available for the purpose of meeting the accrued interest and sinking fund payment on all bonds of the company for that quarter, for during the very time within which the alleged earnings of $554,021.45 had been made by the subsidiary companies, and which the statement infers were available for the payment of all accrued interest and sinking fund charges, they had been compelled to advance in cash to the constituent companies the sum of $424,467.59.

On this showing the application to list the securities was granted by the New York Stock Exchange on January 14th, 1903. A little over four months later, on the 25th day of May, 1903, a statement was issued to the public embodying a plan for the reorganization of the United States Shipbuilding Company upon a basis that would enable it to exist. This proposed plan of reorganization stated that "by reason of the excessive mortgage obligations of the United States Shipbuilding Company, its

borrowing capacity and credit has become so seriously affected that outstanding notes are being pressed for payment and the making of further loans is rendered impossible," and recommended that the Company should be reorganized upon a basis of almost 40 per cent less than was originally considered the fair value of the plants. If other evidence than the figures above set forth be needed to prove that vendors and promoters of this scheme sought to secure stocks and bonds of the United States Shipbuilding Company without consideration, it is supplied by this proposed Plan of Reorganization, which practically states that the Company is unable to pay interest on a greater capitalization and bond issue than $43,000,000, an amount $1,487,000 less than the capital of the United States Shipbuilding Company distributed in connection with the purchase of the properties, to say nothing of the bond issues of $24,500,000.

Causes of Failure

What were the causes of failure of the United States Shipbuilding Company? One of such causes was the fact that the directors parted with bonds to an amount upon which it was impossible to meet the interest. The failure, however, was precipitated, if not directly brought about, by the fact that in the Bethlehem transaction the United States Shipbuilding Company officers had to deal with people who, while thoroughly understanding the intricacies of "higher finance," seemed to have overlooked the requirements of common fairness. In speaking of plant values elsewhere in this report, the Bethlehem property has been dealt with as though it had been purchased by the United States Shipbuilding Company, but an examination of the transaction will show that it was otherwise. While the agreed price for the Bethlehem company was $9,000,000, to be paid for by an issue of $10,000,000 of bonds at 90, the directors of the United States Shipbuilding company, upon request, handed over to Mr. Charles M. Schwab an additional amount of $20,000,000 in the common and preferred stock of the United States Shipbuilding Company. As this $20,000,000 of stock would not be sufficient to give Mr. Schwab the control of the United States

Shipbuilding Company, there was inserted in the mortgage given to secure his $10,000,000 of bonds, a provision that such bonds should have a voting power equal to $10,000,000 of stock. As the total issue of stock of the United States Shipbuilding Company was but $45,000,000, the $30,000,000 voting power thus given to Mr. Schwab was sufficient to justify him in saying that he did not sell the Bethlehem Steel Company, but took over the United States Shipbuilding Company, the directors of that Company giving him $30,000,000 in stock and bonds for taking it off their hands.

In this deal Mr. Schwab parted with nothing. In the sale of the other constituent companies, the real and personal property, as well as their capital stock, were transferred to the United States Shipbuilding Company by the necessary deeds, bills of sale, and assignments. But in the case of Bethlehem, Mr. Schwab permitted to be given up only its capital stock, and this he did in such manner as to place it beyond the control of the Shipbuilding company. If interests friendly to the United States Shipbuilding Company had controlled this stock, it would have been able to reach the earnings of the Bethlehem Steel Company through a friendly Board of Directors; but in the $10,000,000 mortgage it was provided that the Trustee should designate three of such directors, and the United States Shipbuilding Company should designate four. As Mr. Schwab controlled the United States Shipbuilding Company, by reason of his aforesaid majority of stock, and as the Trustee was of his own selection, the United States Shipbuilding Company was absolutely at the mercy of Mr. Schwab. His advisers, however, in evident fear that something had been overlooked, caused the United States Shipbuilding Company to execute a contract wherein it agreed and guaranteed that so long as any part of the $10,000,000 issue of bonds above referred to should be outstanding and unpaid, the Bethlehem company should pay dividends on its entire outstanding capital stock at the rate of not less than six per cent per annum, and for the purpose of making such payments the Shipbuilding company agreed that the Bethlehem company should earn, over and above its operating expenses and fixed charges (including interest on its bonds and taxes), and over and above the working capital of

$4,000,000 therein provided for, a sum sufficient to make such annual dividend disbursements; and, in the event of the failure of the Bethlehem company earning sufficient to pay such dividend at the rate of six per cent, then the United States Shipbuilding Company was to pay to the Bethlehem company, on demand, a sum sufficient to make such annual dividend disbursements. The Shipbuilding company further agreed to supply the Bethlehem company with all such orders, contracts, work and earning capacity as should be necessary to enable it to earn and pay the annual dividends above mentioned. Was ever such another agreement, so apparently harmless, yet so ruinous, conceived by the mind of man? On its face it was simply an agreement to the effect that if sufficient earnings were not made by the Bethlehem to pay a dividend of 6 per cent on its capital stock, the United States Shipbuilding Company would advance such sum. This agreement was an absurd arrangement, in view of the fact that the United States Shipbuilding Company was the nominal owner of this stock, and as such was entitled to its dividends; nevertheless the United States Shipbuilding Company was made to agree in effect that if it wanted dividends from Bethlehem it should contribute the means to enable the payment of such dividends. An excuse for the United States Shipbuilding Company officials entering into such an agreement might be found in the supposition that they may have believed that as they had the right to designate four of the seven directors of the Bethlehem Steel Company, they would be able to control the earnings of that company, and the agreement above mentioned might become inoperative. Such a belief, however, had no substantial foundation, for, as heretofore stated, the control both of the Bethlehem and the United States Shipbuilding Company was vested in Mr. Schwab. Your Receiver will not attempt to advance any reason why the latter thought it necessary to take any such agreement in view of the fact that he had previously thereto obtained a control of the Shipbuilding company that would enable him at any moment to throttle it. As if the foregoing provisions in said agreement were not sufficient, the United States Shipbuilding Company was further made to agree that in the event that the working capital of the Bethlehem Steel Company should at any

time fall below $4,000,000, the United States Shipbuilding Company would, upon demand, make up such sum as might be necessary to bring the working capital up to that figure. The agreement contains other provisions, all operating against the United States Shipbuilding Company, but enough has been referred to to show that in signing it the United States Shipbuilding Company had lost all chance of ever reaching the earnings of the Bethlehem Steel Company. For, assuming that Mr. Schwab's directors of the United States Shipbuilding Company should demand of Mr. Schwab's directors of the Bethlehem Steel Company that a dividend be declared from the earnings of the latter company, Mr. Schwab's directors of the Bethlehem Steel Company could always reply (as they did when demand was made) that it was not considered wise to declare a dividend at that time.

In April, 1903, it became apparent that unless funds were advanced by the Bethlehem Steel Company for the purpose of meeting the semi-annual interest on the first mortgage bonds due July 1st, a default in the payment thereof would ensue. Notwithstanding the urgent need apparent at that time for retrenchment, and the necessity for requiring Bethlehem to set aside some of its large earnings for the purpose of meeting the coming interest, the Executive Committee of the United States Shipbuilding Company, on the 7th day of April, 1903, adopted a resolution approving a report of the president of the Bethlehem Steel Company with reference to certain improvements and extensions alleged to have been required at the works of the latter company, showing a total required expenditure of $2,802,000 (including $365,000 previously appropriated). On the 14th day of April, 1903, the directors of the United States Shipbuilding Company held a meeting, at which time it was sought to approve the minutes of the previous meeting of the Executive Committee. On a motion to approve such minutes, Mr. Lewis Nixon, the president of the company, stated that he desired to go on record concerning the resolution passed, to the effect that in providing for any such extensions and improvements it should be made a condition of any such expenditure that proper provision should be made to safeguard the amount of $900,000, which must be declared as a dividend by the Bethlehem company, and

suggested that provision to that effect be added to the authority asked for. Notwithstanding this request of Mr. Nixon, the minutes of the Executive Committee were approved by the directors.

Your Receiver is informed, and believes it to be true, that thereafter Mr. Lewis Nixon repeatedly sought to induce the directors of the United States Shipbuilding Company to coöperate with him in compelling the Bethlehem company to pay over some of its earnings for the purpose of staving off the impending default of the United States Shipbuilding Company; but from the 14th day of April, 1903, until the 22d day of June, 1903, it was impossible to obtain a quorum either of the Executive Committee or of the directors of the United States Shipbuilding Company. Again, on the 27th of June, while the proceedings were pending in this court for the appointment of a Receiver, Mr. Nixon demanded the Bethlehem Steel Company's assistance for the purpose of averting the impending default, through the medium of the following letter:

NEW YORK, June 27th, 1903

E. M. MCILVAIN, ESQ.,
President Bethlehem Steel Company,
South Bethlehem, Pa.:

DEAR SIR—The Bethlehem Steel Company, having earned during the year ending August 1st, 1903, over and above its operating expenses and fixed charges (including interest on its bonds and taxes), and without impairment of its working capital of $4,000,000, a sum sufficient to pay a dividend of 6 per cent on its entire present outstanding capital stock, I request and demand, in behalf of the United States Shipbuilding Company, as owner of all of said capital stock, that your company, on or before June 30, 1903, declare a dividend in an amount sufficient to pay a bond interest of $362,500, due July 1st, 1903, and pay the same as required by the terms of the agreement of August 12th, 1902, between your company and the United States Shipbuilding Company, and credit this upon the yearly dividend on the stock of the Bethlehem Steel Company, $250,000 of which has already been declared and paid in a similar manner to meet the interest on the twenty-year bonds.

Yours truly,
(Signed) LEWIS NIXON,
President

No attention was paid to this demand, and the default followed. Had the efforts of Mr. Nixon been successful, the subsequent adjudication of insolvency and the appointment of a receiver would have been averted.

Your Receiver considers it his duty to bring to the attention of the Court the fact that while the Bethlehem company was earning upwards of $2,000,000 annually, these earnings were being placed beyond the reach of the United States Shipbuilding Company by the making of vast extensions and improvements in the Bethlehem company and the purchasing and ordering of enormous quantities of merchandise, with the apparent purpose of bringing about the destruction of the United States Shipbuilding Company.

Further proof in this behalf is supplied by Mr. E. M. McIlvain, President of the Bethlehem Steel Company, in his letter to Mr. George R. Sheldon, Chairman of the Reorganization Committee. In this letter, dated the 25th of May, 1903, Mr. McIlvain states that during the fiscal year of the Bethlehem Steel Company ending April 30th, 1903, the net earnings of his company were $2,518,264.58. In the third paragraph of this letter he states that for the year beginning May 1, 1903, a conservative estimate of the net earnings of the Bethlehem Steel Company would be about $2,250,000 after deducting $517,550 of earnings for the purpose of paying interest on the underlying mortgages. Of this amount of earnings, he states, in the fourth paragraph of his letter, that he feels confident that there could be withdrawn for distribution (for dividends) the sum of $1,200,000. During the year within which Mr. McIlvain says the net earnings of the Bethlehem Steel Company were $2,518,264.58, the utmost that the Bethlehem Steel Company could be induced to give up to the United States Shipbuilding Company was $250,000. But in presenting the matter to the public, through the medium of the Reorganization Committee, and with a view to inducing the acceptance of a plan that would further the interests of Mr. Schwab, he states that from the earnings which are not in excess of the fiscal year ending April 30, 1903, he would be able to withdraw and pay over to the reorganized company a sum almost five times as much as his company was able to do when there

was the utmost need for its greatest contribution. Your Receiver is unwilling to believe that Mr. McIlvain would deliberately make a false statement in this connection. He is also willing to accept his statement that the Bethlehem company would be able to withdraw from its current assets the sum of $1,200,000 for distribution during the year beginning May 1, 1903, but in accepting this statement and considering it in connection with the fact that all Bethlehem would advance during the past year was $250,000, and bearing in mind that the major part of the improvements and extensions above authorized were to be completed in subsequent years, it is difficult to draw any other conclusion than that the earnings of Bethlehem company during the past year were deliberately withheld for the purpose of wrecking the United States Shipbuilding Company. During the year ending July 31, 1903, Bethlehem expended for additions to its plant the sum of $683,370.24. In addition to this amount it expended for extraordinary and general repairs, during the year ending April 30, 1903, according to the report of Price, Waterhouse & Co., the sum of $450,000. It increased its material (unfinished and finished product and stores) $687,149.16. Its notes payable, which amounted to $350,000 when the stock of this company was attempted to be purchased by the United States Shipbuilding Company, were reduced $200,000 up to August 1, 1903, and have since been entirely wiped out, and finally it reduced its accounts payable to the extent of $179,468.22. Why such enormous sums should be expended for additions, repairs, and material at a time when the United States Shipbuilding Company was in urgent need of financial aid can be reasonably accounted for only upon the theory that it was in conformity with a deliberate plan to provide a plausible excuse for having withheld all dividends when the crash should come in the affairs of the United States Shipbuilding Company. Some attempt has been made by Bethlehem to justify its retention of its earnings by the statement that its credit had become impaired, and it was therefore necessary to pay cash for supplies, as well as to reduce its accounts and bills payable in order to placate its creditors. The alleged cause of the impairment of credit was said to be a mortgage for $10,000,000 which the

Bethlehem company made to the Colonial Trust Company upon its plant and property at the time of the purchase of Bethlehem by the United States Shipbuilding Company. As further security to Mr. Schwab for the $10,000,000 of bonds delivered to him as the purchase price of Bethlehem, the Bethlehem Steel Company executed to the Colonial Trust Company the mortgage above referred to to secure a bond in the like amount. Your Receiver is advised that the execution and delivery of such bond and mortgage by Bethlehem to secure Mr. Schwab for the purchase price of the sale of the stock of the Bethlehem was a fraud upon the creditors of said company, and was otherwise void because of the control of the directors by Mr. Schwab. In addition thereto, it is evident that the impairment of credit, if any, which Bethlehem complains of, was the result of its own deliberate, unwarranted, and illegal act. Your Receiver submits, therefore, that there was no justification for withholding from the United States Shipbuilding Company the entire earnings of the Bethlehem company, and charges that the inability of the Shipbuilding company to continue its business was due in large part to the failure of the Bethlehem company to relinquish its earnings.

At this point your Receiver desires to call the attention of the Court to another matter somewhat small in comparison with the enormous and unlawful appropriation of stocks and bonds of the United States Shipbuilding Company above mentioned, but of some importance in showing the manner with which the Bethlehem company dealt with the United States Shipbuilding Company. At the time of the sale of the Bethlehem Steel Company to the United States Shipbuilding Company, a statement was made that the amount of inventory was a certain figure. After the sale of the Bethlehem company to the United States Shipbuilding Company, $250,000 of this amount was charged off by the Bethlehem company, for the purpose of adjusting the book value of the inventory with the actual value which had been placed thereon by the accountants after examination. This examination had been made in April, 1902, and the Bethlehem company had been instructed at that time to charge off, to adjustment of inventory, $609,541.95. Instead of complying

with this request, they charged off only $359,541.95, and at the time of the sale of the plant to the United States Shipbuilding Company the statement submitted contained a surplus $250,000 in excess of what Bethlehem knew to be the actual amount.

Still another matter should be brought to the attention of the Court. On the 22d of June, 1903, while proceedings were pending for the appointment of a receiver of the Shipbuilding company, and, as it seems to your Receiver, with a view of forestalling the action of the Court, and in contempt thereof, the directors of said Company adopted a resolution, as provided for under Mr. Schwab's mortgage, requesting the New York Security Trust Company to vote the entire shares of the capital stock of the Bethlehem Steel Company in favor of and for the following persons, as directors of said Bethlehem Steel Company, namely, E. M. McIlvain, Archibald Johnson, Adolphe E. Borie, and Lewis Nixon. Mr. McIlvain was at that time and is now the President of the Bethlehem Steel Company; Mr. Borie was and is the Vice-President of the Bethlehem Steel Company, and Mr. Johnson was and is the General Superintendent of said Company. As the remaining directors were selected by Mr. Schwab's trustee, it is apparent that but one of the seven could be said to represent interests other than those of Mr. Schwab. By this means, if successful, Mr. Schwab was able to place the control of Bethlehem beyond the reach of the Court for at least another year.

Bethlehem Steel Company

From the reports submitted by the officials of this Company, it is evident that during the past year it earned far more money than the necessities of the plant required to be retained there. From what is hereinabove set forth, it is also evident that so long as the present Board of Directors, or a Board subject to present influences, shall retain office, no benefit shall ever be permitted to escape to the Receivership. Your Receiver is convinced that the present controlling influence at this plant is wholly hostile to the Shipbuilding company and its representatives, and your Receiver believes, in view of the excessive price paid for its plant, that the Shipbuilding company, or its repre-

sentative, should be permitted to have at least some voice in its management. At present this is denied, but your Receiver hopes that such action may be taken as may result in the removal of the present Board of Directors, or a majority of them. Your Receiver believes that the meeting of the Board of Directors of the United States Shipbuilding Company, held on the 22d day of June, 1903, and hereinbefore referred to, at which four directors were designated to represent the United States Shipbuilding Company on the Board of the Bethlehem Steel Company, was solely for the purpose of circumventing any order of this Court which might be made in the proceedings then pending; that it was intended to hinder and delay the creditors of the United States Shipbuilding Company and to place this property beyond their control and the control of the Receiver to be appointed, and was otherwise illegal and void. Your Receiver believes such Board is deliberately furthering a course at once illegal and greatly injurious to the creditors represented by your Receiver, and accordingly he makes the recommendation concerning this Company hereinafter set forth.

Generally

Since the appointment of your Receiver the principal office has been engaged in legal matters rather than building ships. Accordingly your Receiver found the services of several of the officers and subordinates of the Shipbuilding company to be unnecessary, and in this connection has reduced expenses upwards of $55,000 a year.

Recommendations

Your Receiver respectfully submits the following recommendations:

1. That in order to avoid depreciation by disuse, and because of the existence of controversies as to the validity of the encumbrances upon the premises, the Crescent Shipyard be sold free and clear of all such encumbrances as soon as the work now in contemplation is completed.

2. That similar action be taken with reference to the plant

of the Harlan & Hollingsworth Company, Wilmington, Delaware.

3. That as soon as the debts of the company shall have been ascertained suit be instituted against all persons who received the stock of this company without paying full value therefor to recover from them such an amount as shall be necessary to pay said debts in full, under section 21 of an act of the Legislature of the State of New Jersey, entitled, An Act concerning Corporations (Revision of 1896).

4. That suit be instituted against the Bethlehem Steel Company to procure the appointment of a Receiver and to compel the appropriation of the earnings of that company by way of dividends on the stock.

Respectfully submitted,

JAMES SMITH, JR.,

Receiver, United States Shipbuilding Company

Dated October 31, 1903.

Certain other highly disreputable details of this affair were concerned with the attempts to float the stock in Europe. Much of the correspondence, showing connivance with notorious parties in Paris, was published in the New York daily papers between December 22, 1903, and the first of January, 1904. Moody's Truth about the Trusts, pp. 366–369, gives many additional details. A paper by L. W. Sammis of the *New York Sun*, published in the Annals of the American Academy of Political Science, 1904, is also suggestive. After protracted controversy and litigation, a reorganization plan was agreed upon and published May 25, 1905; and a new company was formed to take over the wreck of the old one. Dewing, *op. cit.*, should be consulted for details. — ED.

NOTE. A more impartial account will be found in Dewing's Corporate Promotions and Reorganizations, 1914, chapter XVIII. At p. 505 he alleges this was practically a partisan document. It is the official Receiver's report, nevertheless, and affords admirable matter for debate. The teacher should read Dewing carefully.

XIII

THE ASPHALT COMBINATION[1]

THE visible assets of Asphalt Company of America having been sold and their proceeds distributed, . . . it is proper that the Court should be informed of certain matters and things relating to the promotion of Asphalt Company of America, for such action thereupon as the Court may determine should be taken. The facts hereinafter set forth have been ascertained through investigations made by the Receivers continuing from immediately after their appointment up to the present time.

Asphalt Company of America was incorporated under the laws of the state of New Jersey, June 28, 1899, with an authorized capital stock of $30,000,000, divided into 600,000 shares of the par value of $50 each. The corporation was the outcome of plans previously arranged by and among some or all of the persons hereinafter mentioned as promoters, the essential features of which were (1) the transfer to the corporation of the shares of stock of certain other corporations engaged in the asphalt business and more or less competitive in character, and the issue to the owners of such shares, so transferring their holdings, of Collateral Gold Certificates, in the nature of bond obligations of the new corporation in exchange for said shares of stock, the terms of exchange being mutually arranged, the shares of stock so transferred then being deposited with a trust company (The Land Title and Trust Company being selected) as security for the payment of the interest and principal of the said certificates. (2) The providing of working capital

[1] From Transcript of Record, U. S. Circuit Court of Appeals for the Third Circuit, September Term, 1903. *The Land Title and Trust Co.* v. *Henry Tatnall as Receiver of Asphalt Co. of America*, etc., pp. 370–380. Receiver's Report on Promoters' Liability, etc. A more adequate account of the affair will be found in A. S. Dewing, Corporate Promotions and Reorganization, Harvard Economic Studies, 1914, chapter XV. The economic background will be especially appreciated by the teacher.

for the new corporation by calls upon its capital stock. In the case of the transfer of the shares of stock by some of the said companies to the new corporation, it was stipulated that, in addition to the purchase price to be paid in Collateral Gold Certificates, the vendors should have the privilege of purchasing stock of Asphalt Company of America, without premium at par, to the amount of 50 per cent of the par value of the stock deposited by them. The following is a list of the corporations whose shares of stock to the amounts and on the terms therein stated were transferred to Asphalt Company, and Collateral Gold Certificates, to the amounts therein mentioned paid therefor:

Name of Company	Total No. of Shares	Par Value	Shares Purchased	Price Paid	Cost in Cash	Cost in Certificates
Barber Asphalt Paving Company	39,000	$100.00	38,993	$300.00	——	$11,697,900.00
The New Trinidad Lake Asphalt Company	50,000	48.50	49,550	100.00	——	4,955,000.00
			50	84.886	$4244.32	——
Alcatraz Company of West Virginia	800,000	5.00	799,900	6.00	——	4,799,400.00
United Asphalt Company	40,000	100.00	39,975	91.808	——	3,670,000.00
Atlantic Alcatraz Asphalt Company	1,000	100.00	995	1000.00	——	995,000.00
Southern Asphalt Paving Company	250	100.00	245	1020.00	——	249,900.00
Alcatraz Paving Company	1,000	50.00	995	500.00	——	497,500.00
Alcatraz Asphalt Paving Company	1,000	100.00	995	150.00	——	149,250.00
Warren-Scharf Asphalt Paving Company	9,500	100.00	9,483	240.00	5618.42	2,278,320.00
Utica Paving Company	250	100.00	245	510.21	——	125,001.45
Denver Paving Company	35,000	1.00	34,950	5.714	——	199,714.09
Southwestern Alcatraz Asphalt & Construction Company	2,000	100.00	1,995	64.16	——	127,999.20
Alcatraz Construction Company	1,500	100.00	1,495	104.31	——	155,943.45

The evidence in the possession of the Receiver shows that the persons who transferred to Asphalt Company of America the shares of stock in the above named corporations, receiving Col-

lateral Gold Certificates of the former company therefor, had been holders of shares of stock of some of the companies prior to the inauguration of the plan which was subsequently consummated of transferring them to Asphalt Company of America. In the case of some of the companies, however, some of the vendors who were connected with the organization of Asphalt Company of America as promoters, purchased the whole or some part of the shares which they exchanged for Collateral Gold Certificates on the above terms, after they, with others, had determined upon such organization and either while it was in process of organization or after it was actually incorporated. The essential purpose of this report is to show to the Court the facts which have come to the Receiver's knowledge as to those purchases, and to recommend action thereon.

The organization of Asphalt Company of America appears to have been under consideration as early as March 6, 1899, and to have been entered upon very shortly thereafter. At that time the following persons appear to have been holders of record of shares of stock of some of the corporations which were subsequently combined in the manner above stated, to about the following amounts:

	Barber Asphalt Paving Company	The New Trinidad Lake Asphalt Company
	Shares	Shares
Amzi L. Barber held	5507	4394
Francis V. Greene held	900	1822
George W. Elkins held	1831	1639
J. J. Albright held	2613	3050
Edmund Hayes held	1264	2131
C. K. Robinson held	281	997
E. Burgess Warren held	5164	4849
Wm. L. Elkins held	500	—
Geo. D. Widener held	1091	1273

	Alcatraz Company of West Virginia	Denver Paving Company
	Shares	Shares
William H. Crocker held	401,320	1863

	ALCATRAZ PAVING COMPANY	SOUTHWESTERN ALCATRAZ & CONSTRUCTION COMPANY
	Shares	Shares
William J. Latta held . .	30	—
Harry C. Spinks held . .	—	585

Some of the above named parties then acquired shares of stock of other companies subsequently turned into the combination, and they also acquired more shares of stock of some of the companies in which they already had interests. Some of the shares of stock so acquired were then transferred to Asphalt Company of America, when incorporated, at prices payable in Collateral Gold Certificates in excess of the prices at which they were respectively obtained by the purchasers, and the Receiver believes that further investigation will show that all of said shares were transferred by the said purchasers to Asphalt Company of America at a profit. So far as the Receiver knows, no disclosure to Asphalt Company of America was made by the persons who so transferred their shares of stock to it of the profits received by them. All of the above named parties, it is believed, were beneficially interested in the acquisition of some of said shares, and in their transfer to Asphalt Company of America.

The facts in detail for the consideration of the Court follow:

As to United Asphalt Company.

Amzi L. Barber, Francis V. Greene and George W. Elkins each transferred to Asphalt Company of America 13,325 shares of stock of this company, aggregating 39,975 shares. Amzi L. Barber and George W. Elkins each received therefor $1,223,300, and Francis V. Greene received $1,223,400, in Collateral Gold Certificates of Asphalt Company of America, the said three parties receiving as a whole $3,670,000 of said certificates. At the time of said transfers United Asphalt Company was the holder, either in its corporate name, or by its representatives, of practically the entire capital stock of four corporations known as Columbia Construction Company, of New York; Trinidad Bituminous

Asphalt Company, of New Jersey; Standard Asphalt Company, of New Jersey, and Rock Creek Natural Asphalt Company of Kansas. The shares of capital stock of these corporations constituted its entire assets. The evidence in the possession of the Receiver points to the fact that these shares of stock were bought by or under the direction of Amzi L. Barber, Francis V. Greene and George W. Elkins, with money or obligations furnished, or procured, by them to be furnished as follows:

For the stock of		Columbia Construction Company	$250,000
"	"	Trinidad Bituminous Asphalt Company	150,000
"	"	Standard Asphalt Company	200,000
"	"	Rock Creek Natural Asphalt Company	18,000
			$618,000

Said purchases were made between March 21 and August 4, 1899. In the meantime United Asphalt Company had been organized as a holding company, and on July 12, 1899, 13,325 shares of its capital stock were issued to Amzi L. Barber, Francis V. Greene and George W. Elkins each, making 39,975 shares in the aggregate, issued to them out of a total capital stock of 40,000 shares. The above 39,975 shares were subsequently, on July 15, 1899, transferred to Asphalt Company of America for $3,670,000 of its Collateral Gold Certificates. The first sales of the Temporary Certificates standing for said Collateral Gold Certificates were in August, 1899, in the neighborhood of 90 per cent of par. Taking the value of the Collateral Gold Certificates at 97 per cent of par, the highest price at which said certificates sold, the profit each of the said three parties to said transaction was about $980,601, and to all of them together was about $2,941,803. Taking the value of the said certificates at 89½ per cent of par, which was their lowest market price in August, 1899, the profit to each of said parties was about $888,853.50, and to all of them together was about $2,666,560.50.

As to Warren-Scharf Asphalt Paving Company.

Amzi L. Barber, Francis V. Greene and George W. Elkins each transferred to Asphalt Company of America 3164 shares (George W. Elkins transferring 3165 shares) of stock of Warren-Scharf Asphalt Paving Company, aggregating 9493 shares

out of a total capital stock of 9500 shares. They each received therefor $759,360 (George W. Elkins receiving $759,600) in Collateral Gold Certificates. The said three persons received as a whole $2,278,320 par of said certificates.

The said three persons had previously purchased from the then owners the said shares of stock at an outlay to them of about $1,500,000, and the said shares were transferred into their names on July 27, 1899. The transfers of said shares by them to Asphalt Company of America were made on July 31, 1899, and the above mentioned temporary certificates of said company were issued to them therefor. Taking the value of the Collateral Gold Certificates at 97 per cent of par, the profit to each of the said three parties to said transaction was about $236,579, and to all of them together was $709,970. Taking the market value of the certificates at 89½ per cent of par, the profit to each of the said parties was about $179,627.20, and to all of them together about $539,096.

From certain papers in the possession of Receiver it would appear that the moneys necessary to purchase said shares of stock from the preceding holders were contributed by the following parties in the following proportions, and the Receiver believes that distribution of Collateral Gold Certificates was made to said parties in proportion to their contribution to purchase money as follows, and that they shared the profits proportionately:

	Payment of Purchase Money	Distribution of Collateral Gold Certificates
J. J. Albright	$115,875	$176,130
A. L. Barher	233,175	334,426
F. V. Greene	50,550	76,836
Edmund Hayes	64,950	98,724
C. K. Robinson	20,325	30,894
Geo. D. Widener	49,800	75,696
E. B. Warren	215,325	327,294
Geo. W. Elkins	250,000	380,800
Wm. L. Elkins	250,000	380,000
Sydney F. Tyler	250,000	380,000

As to The New Trinidad Lake Asphalt Company, Limited.

Shortly after the organization of Asphalt Company of America was projected, the Board of Directors of Barber Asphalt Company, which company owned 1718 shares of the capital stock of The New Trinidad Lake Asphalt Company, Limited, caused said shares to be offered for sale to its stockholders. This action was taken pursuant to the authorization of its Executive Committee, acting as a Board of Directors, on March 15, 1899, and was approved by the Board on March 29, 1899, the said Board of Directors being composed at the time of the following persons: J. J. Albright, Amzi L. Barber, Francis V. Greene, Edmund Hayes, C. K. Robinson, George D. Widener, George W. Elkins, E. Burgess Warren, and P. W. Henry. 1638 of the said shares of stock of The New Trinidad Lake Asphalt Company, Limited, were thereupon bought by the stockholders of Barber Asphalt Paving Company at the limit fixed by the Executive Committee in its resolution for their sale, to wit, $48.50 per share. 1515 of the said shares so bought were purchased and paid for by the following persons who were also Directors of Barber Asphalt Paving Company at the rate of $48.50 per share, to wit:

J. J. Albright	210	shares
Amzi L. Barber	206	"
Francis V. Greene	178	"
Edmund Hayes	209	"
C. K. Robinson	103	"
George D. Widener	207	"
George W. Elkins	211	"
E. Burgess Warren	211	"

After said purchases of said shares of stock at $48.50 per share, they were transferred to Asphalt Company of America at the valuation of $100 per share and Collateral Gold Certificates were received in exchange therefor to the amount in the aggregate at par of $151.500.

The Receiver believes it can be established that the said parties shared in the profits of said purchases and sales in proportion to their said holdings.

Taking the Collateral Gold Certificates at 97 per cent of par, the profit to said parties from the said purchases and transfers

amounted to $73,477. Taking the value of the Collateral Gold Certificates at 89½ per cent of par, the profit to the said parties amounted to $62,515.

As to Alcatraz Company.

William H. Crocker transferred to Asphalt Company of America on or about August 3, 1899, 799,650 shares of the capital stock of Alcatraz Company of West Virginia. Prior to the formation of the plan of organization of the Asphalt Company of America the said Crocker was the holder of record of 401,320 shares of said company, the balance of the holdings transferred by him to Asphalt Company of America, to wit, 398,330 shares, having been acquired by him after March 8, 1899. The Receiver has not as yet been able to obtain information as to the amount paid by the said Crocker for said 398,330 shares transferred into his name after the organization of Asphalt Company of America was determined upon, nor what profit, if any, was made by him on the purchase or other acquisition by him of said shares and the sale thereof to Asphalt Company of America. The said shares, with the other shares previously held by him ($5 par value), were transferred to Asphalt Company of America at the rate of $6 per share, payable in Collateral Gold Certificates. The actual sum received by him in Collateral Gold Certificates for the shares obtained by him after the plan of organization of Asphalt Company of America was determined upon was at par $2,389,980. The Receiver has reason to believe that a substantial profit was made by the said Crocker in said transaction. He is advised that the relation of the said Crocker to the enterprise was that of a promoter, and that whatever profit was obtained by him he is in law obliged to pay to the Receiver of the Asphalt Company of America.

As to Denver Paving Company.

The said William H. Crocker transferred to Asphalt Company of America 28,725 shares of Denver Paving Company stock at the rate of $5.71 428/1000 per share (the shares being $1 par) and received in exchange therefor at par $164,142.69 in Collateral Gold Certificates. He was the holder of record prior to the

formation of the plan of organization of Asphalt Company of America of only 1863 of said shares. The balance of his holdings transferred to Asphalt Company of America as aforesaid, 26,862 shares, appears to have been acquired by him after the plan of organization of Asphalt Company of America was entered upon. The actual sum received by him in Collateral Gold Certificates for said shares, so as aforesaid subsequently obtained, was at par $153,496.98. The Receiver has reason to believe that a substantial profit was made by the said Crocker in the said transaction. He is advised that the relation of the said Crocker to the enterprise was that of a promoter, and that whatever profit was obtained by him, he is in law obliged to pay to the Receiver of Asphalt Company of America.

As to Alcatraz Paving Company.

William J. Latta transferred to Asphalt Company of America, in July, 1899, 305 shares of Alcatraz Paving Company ($100 par) at the rate of $500 per share, payable in Collateral Gold Certificates of Asphalt Company of America. The actual sum received by him for the said shares, payable in Collateral Gold Certificates at par aforesaid, was $152,500. Prior to the formation of the plan of organization of Asphalt Company of America the said Latta was the holder of record of only 30 of said shares of stock. He appears to have acquired 275 of the shares transferred to Asphalt Company of America as aforesaid after said date. The actual sum received by him in Collateral Gold Certificates for said 275 shares was $137,500. The Receiver has reason to believe that a substantial profit was made by the said Latta in said transaction. He is advised that the relation of the said Latta to the enterprise was that of a promoter and that whatever profit was obtained by him he is in law obliged to pay to the Receiver of Asphalt Company of America.

As to Southwestern Alcatraz Asphalt & Construction Company.

Harry C. Spinks transferred to Asphalt Company of America on or about August 10, 1899, 1995 shares of the stock of the Southwestern Alcatraz Asphalt & Construction Company at the rate of $64.16 per share, payable in Collateral Gold Certificates

of Asphalt Company of America. He received therefor in said certificates at par $127,999.20. The said Spinks actually held of record prior to the entry upon the plan of organization of Asphalt Company of America only 585 of said shares. The evidence in the Receiver's possession indicates that he obtained from various other persons after said date 1410 of said shares which he transferred to Asphalt Company of America upon the total consideration payable in Collateral Gold Certificates at par $90,465.60. The Receiver has not as yet been able to ascertain what profit the said Spinks made out of the purchase of said shares and the transfer thereof to Asphalt Company of America. He is advised, however, that the relations of the said Spinks to the organization of Asphalt Company of America were such that he is obliged to account for and pay over whatever profit he obtained in connection with the said transaction.

From the facts which have come to the knowledge of the Receiver he believes that some or all of the parties above named, to wit, Amzi L. Barber, Francis V. Greene, George W. Elkins, J. J. Albright, Edmund Hayes, C. K. Robinson, E. Burgess Warren, William L. Elkins, George D. Widener, Sydney F. Tyler, William H. Crocker, William J. Latta and Harry C. Spinks, can be established to have been promoters of Asphalt Company of America, and that they made profits in connection with its organization in the manner above stated, which they are obliged to account for, and that they can be compelled to account for and pay over the same. He therefore recommends, the premises considered, that he be authorized by the Court to take such proceedings against the said parties, or any of them, by suit or suits in law or equity, as he may be advised are proper, and as he may deem expedient under the facts as they exist and shall be made to appear upon further investigation, with a view to collecting all profits that were made by the said persons, or any of them, in connection with the organization of Asphalt Company of America and the transfer of securities to it. He also recommends that he be authorized to bring like proceedings against any other persons whom he may hereafter ascertain to have obtained such profits.

He respectfully calls attention of the Court to the fact that

an Act of Limitation was passed by the Legislature of the state of New Jersey at the last session, approved the 8th day of April, 1903, which limits the period during which suits may be brought against directors, officers, promoters and other agents of corporations of the state to recover unlawful profits made by them, to the period of four years from and after the making or receipt of such profits. A saving clause being, however, incorporated in the said Act which permits such suits which otherwise would be barred to be brought within six months after the Act took effect. The result of the passage of the said Act is that proceedings against promoters in connection with Asphalt Company of America with a view to the recovery of unlawful profits obtained by them as the Receiver is advised, must be begun before October 8, 1903. He therefore respectfully urges upon the Court the desirability, if it should seem proper that the Court instruct that any suits of this kind be brought, that the authorization to him to so proceed be given forthwith.

Respectfully submitted,

HENRY TATNALL,

Receiver Asphalt Company of America

July 6, 1903

It is scarcely to be expected that a company launched under the conditions described in the foregoing report should have a successful career. Two reorganizations promptly followed in less than four years. The original Asphalt Company of America, organized in July, 1899, acquired the stocks of a large number of competing concerns, issuing in payment therefor $30,000,000 of collateral trust bonds. These bonds were issued on the security of the stock so acquired. The next step was to assure the control of the enterprise by the promoters through ownership of a majority of the capital stock. Accordingly practically all of the original stock subscriptions were taken in the name of two dummies. A large part of this issue of original stock was immediately turned over to the promoters, giving them virtual control of the enterprise. The stock was not paid for in full, but an amount equivalent to 20 per cent of the par value, which was $50 per share, was actually paid. The funds to meet this partial payment on the stock held by the promoters were raised by a sale of the balance of the stock not held by insiders to the public at prices ranging as high as $19 per share. Thus did the promoters acquire control of the holding company without any additional investment on their part; and at the same time possess themselves of a volume of bonds, which, on the basis of the excessive payments described in the preceding

report, proved more than sufficient to absorb the entire earnings of the consolidation.

The existence of a stockholders' liability for the remaining four-fifths of the par value of the capital stock was the cause of the speedy reorganization of the company in May, 1900. By reason of fraudulent and reckless accounting, as partially indicated by our preceding reprint, the inevitable bankruptcy of the parent company was hidden from the public temporarily. In brief, the Asphalt Company of America was superseded in May, 1900, by a new company entitled the National Asphalt Company. This new corporation issued $6,000,000 of Collateral Gold Certificates which were used to take up the stock of the old corporation. In addition, its own capital, amounting to $22,000,000, was used in part to acquire control of formidable competitors who had invaded the field, and in part as a bonus to secure deposit of the old underlying bonds. In December, 1901, this company, in turn, went into the hands of a receiver. Then began a long series of suits and countersuits in connection with the activity of a reorganization committee; which, judged by results, seems to have been working in the interest of insiders. The outcome of the matter was the final organization in May, 1903, of the General Asphalt Company which acquired the properties of its predecessors, sold at auction for a trifle over $6,000,000. This General Asphalt Company was capitalized at $31,000,000, in place of $60,000,000 of stock and bonds issued by the original Asphalt Company of America. The troublesome underlying bonds of the first company were to be retired by exchange for preferred stock; and the common stock was issued in part to raise working capital.

A partial recovery of the enormous losses by innocent investors could be effected only in two ways. Successful suits against the promoters for unrevealed profits in the organization of the company might be hoped for, following precedents in a number of recent cases, notably that of the East Tennessee Land Company. In addition it was possible that the Receiver might be able to hold the original stockholders liable for the balance of their payments on the capital stock of the Asphalt Company of America. This latter should amount to about $24,000,000, while at the same time it was hoped that nearly $3,000,000 could be extorted from the promoters. The first of these remedies against the promoters, however, has now been closed through purchase by the promoters themselves of all the outstanding bonds. As representing all the creditors of the company, they have asked the Court to discontinue the suits. This has been done. Moreover, the Receiver has abandoned the attempt to assess the stockholders for their unpaid capital stock on the ground that such suits cannot be successfully prosecuted. Thus closes a story of fraud and financial rottenness not less enlightening than that of the United States Shipbuilding Company, as showing the necessity for provision by law to secure a reasonable amount of publicity in the finances of monopolistic combinations. — Ed.

XIV

TRADE COMBINATIONS AT COMMON LAW[1]

THE rule that all contracts in restraint of trade were void, was early established in the English law. The first case in which this principle was announced is said to have been decided in the reign of Henry V.[2] In this case an action for debt was brought on a bond, conditioned that the defendant should not use his art of a dyer's craft within a certain city for six months. Judge Hall declared the bond void, and expressed his indignation at this attempt to restrain trade by exclaiming, "And, by God, if the plaintiff were here, he should go to prison till he paid a fine to the king." This refusal to recognize the validity of any contract in restraint of trade was for a long time characteristic of the English law; but gradually the rule was relaxed.

The modern application of this rule was very well expressed by Judge Christiancy in the case of *Hubbard* v. *Miller*.[3] Dissenting from the doctrine sometimes laid down, that all contracts in restraint of trade are *prima facie* or presumptively void, he said:

> If, considered with reference to the situation, business and objects of the parties, and in the light of all the surrounding circumstances with reference to which the contract was made, the restraint contracted for appears to have been for a just and honest purpose, for the protection of the legitimate interests of the party in whose favor it is imposed, reasonable as between them, and not especially injurious to the public, the restraint will be held valid.[4]

[1] From the *Political Science Quarterly*, vol. XII, 1897, pp. 212–245. *Cf.* also p. 561 ff., *infra*.

[2] See Year Book, 2 Henry V, fol. 5, pl. 26.

[3] 27 Mich. 15.

[4] This statement was really nothing but an elaboration of the rule which had long before been laid down in the English courts by Chief Justice Tindal, in the case of *Horner* v. *Neves*, 7 Bing. 743.

Under this rule two interests are to be considered, those of the parties to the contract and those of the public. As to the former, the rule was laid down that no contract which did not benefit both parties to the contract should be regarded as reasonable; as to the latter, no contract in restraint of trade was to be regarded as lawful which was injurious to the public. As a matter of fact, most of the cases actually decided have turned exclusively on the interests of the parties, and the tendency of the courts has therefore been to relax very greatly the old rule of the common law. This tendency probably reached its culmination in a case decided in 1887, by the New York Court of Appeals, *Diamond Match Co.* v. *Roeber*.[1] Here the Court was called upon to construe a contract made by Roeber with the Swift, Courtney & Beecher Co., the grantor of the Diamond Match Co., in which he agreed that he would not within ninety-nine years, except in the capacity of agent or employee of the Swift, Courtney & Beecher Match Co., directly or indirectly engage in the manufacture or sale of friction matches in any part of the United States except Nevada and Montana. The Court held the contract to be valid, although practically in general restraint of trade, saying:

When the restraint is general, but at the same time is coextensive only with the interest to be protected and with the benefit meant to be conferred, there seems to be no good reason why as between the parties the contract is not as reasonable as when the interest is partial and there is a corresponding partial restraint.

But the Court of Appeals, in making this decision, did not intend to depart from the old rule, so far as the maintenance of that old rule was necessary for the protection of the interest of the public. It said distinctly:

Covenants of the character of the one now in question operate simply to prevent the covenanter from engaging in the business which he sells, so as to protect the purchaser in the enjoyment of what he has purchased. To the extent that the contract prevents the vendor from carrying on the particular trade, it deprives the community of any benefit it might

[1] 106 N. Y., 473.

derive from his entering into competition; but the business is open to all others, and there is little danger that the public will suffer harm from lack of persons to engage in a profitable industry. Such contracts do not create monopolies; they confer no special or exclusive privilege. If contracts in general restraint of trade where the trade is general are void as tending to monopolies, contracts in partial restraint where the trade is local are subject to the same objection, because they deprive the local community of the services of the covenanter in the particular trade or calling, and prevent his becoming a competitor with the covenantee.

And again:

Combinations between producers to limit production and to enhance prices are or may be unlawful, but they stand on a different footing.

This case has frequently been cited, as indicative of a change in the rule of the common law, and as establishing the proposition that in our present economic conditions the policy of the law is, in order to promote the greatest freedom of contract, not to declare void contracts even in total restraint of trade. But the Court of Appeals based its decision upon the express ground that the public interest was not involved. While holding valid the particular contract before it, although in general restraint of trade, the Court specifically declared that combinations to raise prices stood upon a different footing, and recognized the fact that where the public interest was involved, the rule might well be different. The common law has all along refused, and does now refuse, to recognize the validity of agreements made between individuals for the purpose of raising the prices of commodities, and has stamped any such attempt as a criminal conspiracy.

I. Agreements aiming to raise Prices are Invalid

That such agreements are invalid has always been the rule of both courts of equity and courts of law. Thus, take the case of *Craft* v. *McConoughy*.[1] This was a bill in equity brought for an accounting and distribution of the profits of an alleged partnership based upon a contract to the following effect: Several grain houses were put into the business upon a basis of distribut-

[1] 79 Ill., 346, decided in 1875.

ing shares to the signers of the agreement; each separate firm was to conduct its own business as if there were no partnership in existence. It was to be the duty of a general bookkeeper to make a record of all the grain bought by each party, to debit him with the amount of money paid for the same, and to credit him with all sales; and at the end of every month each individual account was to be balanced, showing the profit or loss, which amount was to be divided *pro rata*, according to the number of shares held by each party. It was further agreed that prices were to be fixed from time to time, and each party to the agreement was to abide by them. Soon after the agreement was made, one party to it died, and his son demanded an accounting. The Court held that the agreement was void, as contrary to public policy, and as being an attempt to foster a monopoly and to raise prices; and notwithstanding the fact that it had been partially executed, refused to require an accounting, saying: "The complainant and the defendants were equally involved in the unlawful combination; a court of equity will assist neither."

A similar and even stronger case, decided in Pennsylvania, is that of *Nester* v. *The Continental Brewing Co.*[1] Here an association had been formed in Philadelphia among the brewers, for the purpose of controlling the sale and fixing the price of beer in Philadelphia and in Camden and Camden County, New Jersey. It was shown that the plaintiff had for valuable consideration obtained from a member of the association an assignment of a claim due such member from the association, without knowledge that the claim was based upon an agreement to monopolize the sale of beer. Notwithstanding his *bona fides*, the Court refused to aid him, and denied his application for an accounting.

Not only courts of equity, but also courts of law, refuse to aid in the execution of such agreements. Thus, in the case of *Chapin* v. *Brown*,[2] the grocers engaged in business in the town of Storm Lake agreed in favor of a third person to quit the business of buying butter for two years, and such third person agreed to carry on that business exclusively for the same period

[1] 161 Pa. St., 473, decided in 1894.
[2] 83 Iowa, 156, decided in 1891.

of time. In pursuance of this agreement, the plaintiffs came to the town and engaged in the business of buying butter; at the commencement of the suit they were so engaged, and had made arrangements to continue the business for the period of two years. The defendant, however, continued in the business of buying butter; and it was alleged that by so doing he had damaged the plaintiffs to the extent of one hundred and fifty dollars, for which judgment was asked. The court refused the application of the plaintiffs, on the ground that the agreement was against public policy, as tending to monopolize the butter trade at Storm Lake, and to destroy competition in that business. This case is particularly interesting because the agreement was as to purchase and not as to sale. It therefore did not result in disadvantage to the consuming public generally, but only in disadvantage to the producers of butter.[1]

A somewhat similar case, *More* v. *Bennett*, was decided in January, 1892, by the Supreme Court of Illinois.[2] Here the stenographers in the city of Chicago had formed an association, of which all the parties to the suit were members. The object of the association was to establish and maintain uniform rates. A schedule had been adopted, and it was alleged that the defendant, contrary to the rules of the association, had cut rates against the other members thereof, whereby the plaintiffs had been damaged. The Court refused to pass upon the question whether a contract could be found in such articles of association, and decided that, even if a contract could be found, the agreement was void on account of its attempt to regulate prices. The Court refused, therefore, to award damages to the plaintiff. The case is interesting as showing that the courts will apply the same rules to the attempt to regulate the price of labor as to the attempt to regulate the price of commodities.

Another good case is that of the *Texas Standard Oil Co.* v. *Adoue*, decided in Texas in 1892.[3] This suit was brought to recover guaranteed net prices for all the products of certain

[1] It is only fair to say that the contract was declared void, not only because it was contrary to public policy, but also because in the opinion of the Court it was not based upon a consideration.

[2] 140 Ill., 69. [3] 83 Tex., 650.

mills, and for the costs and expenses of production, in consideration of the strict performance of all convenants in a contract. This contract, it was held by the Court, gave the defendant an almost unrestricted field to obtain the raw material for its mills, and the exclusive right to control, free from the competition of the plaintiffs and others, not only the sales and ruling prices of the product of its own mills, but also the entire yield of the mills of the other parties to the contract. The Court held that the manifest purpose and natural tendency of this agreement were to prevent competition in too many localities — upon the one hand, to reduce the price of the raw materials; and upon the other, to enhance that of the manufactured product by artificial means, to the disadvantage and detriment of the public. Therefore the complaint was dismissed.[1]

A similar case is *Arnott* v. *The Pittston and Elmira Coal Co.*[2] Here the plaintiff's assignor, the Butler Colliery Co., had made an agreement with the defendants that it would not send coal north to any point except to the defendants, the latter agreeing to take from the Butler Co. not exceeding 2000 tons of coal per month. In pursuance of this agreement, the Butler Colliery Co. shipped 2700 tons to The Pittston and Elmira Coal Co., and the plaintiff, to whom it had assigned its claim, brought suit for the price of the coal. The Court held that the contract was made by the defendants with the purpose of establishing a monopoly of coal in the city of Elmira, that this purpose was known to the plaintiff's assignor, the Butler Coal Co., that the contract was contrary to public policy, and therefore that suit might not be brought upon it. The Court said:

Every producer or vendor of coal or other commodity has the right to use all legitimate efforts to obtain the best price for the article in which he deals. But when he endeavors to artificially enhance prices by suppressing or keeping out of market the products of others, and to accomplish that purpose by means of contracts binding them to withhold

[1] This case, like *Chapin* v. *Brown*, noticed above, shows that the courts will take notice that the effect of a combination in restraint of trade is to reduce the prices of articles to be purchased, as well as to increase the price of articles to be sold by the combination.

[2] 68 N. Y., 558, decided in 1877.

their supplies, such arrangements are even more mischievous than combinations not to sell under an agreed price. Combinations of that character have been held to be against public policy and illegal. . . . The purpose of the vendee was against public policy, and the vendor knew it. This brings us straight to the question whether the vendor delivering goods under such a contract can recover for the price. I think that under the circumstances of the present case, as found by the referee, he cannot. . . . He had a right to dispose of his goods, and (under certain limitations) the vendor of goods may recover for their price, notwithstanding that he knows that the vendee intends an improper use of them, so long as he does nothing to aid in such improper use, or in the illegal plan of the purchaser. This doctrine is established by authority, and is sufficiently liberal to vendors. But — and this is a very important distinction — if the vendor does anything beyond making the sale to aid the illegal scheme of the vendee, he renders himself *particeps criminis* and cannot recover for the price.

So, also, it has been held that a loan made for the purpose of aiding in a combination to raise the price of a particular article, cannot be recovered. In the case of *Raymond* v. *Leavitt*,[1] plaintiff had loaned the sum of $10,000 to the defendant for the purpose of controlling the wheat market at Detroit, with a view of forcing up prices. The defendant, who was to give the plaintiff a third of the expected profits, was at all events to repay the $10,000, with or without profits. In rendering its decision, the Court said:

The object of the arrangement between these parties was to force a fictitious and unnatural rise in the wheat market, for the express purpose of getting the advantage of dealers and purchasers whose necessities compelled them to buy, and necessarily to create a similar difficulty as to all persons who had to obtain or use that commodity, which is an article indispensable to every family in the country. . . . We shall decline enforcing such contracts. If parties see fit to invest money in such ventures, they must get it back by some other than legal measures.

Probably the strongest case of all is that of *Morris Run Coal Co.* v. *Barclay Coal Co.*[2] This was an action upon an accepted draft of the defendants in favor of the plaintiffs. The draft was made in execution of a contract between five coal companies

[1] 46 Mich., 447, decided in 1881.
[2] 68 Pa. St., 173, decided in 1871.

for a sum found due in the equalization of prices under the contract. Provision was made in the contract for a committee of three to take charge of the business of all of these companies, to decide all questions and to appoint the general sales-agent. Provision was also made for the mining and delivery of coal, and for its sale through this agent, subject, however, to the restriction that each party should at its own cost deliver its proportion of the different kinds of coal in the different markets, at such times and to such parties as the committee should from time to time direct. The committee was authorized to adjust the price of coal in the different markets, and the rates of freight, and also to enter into such an agreement with the anthracite coal companies as should promote the interest of the parties. The companies were allowed to sell their coal themselves, but only to the extent of their proportion, and only at the prices adjusted by the committee. In answer to the claim that this agreement tended to establish a monopoly, the plaintiff replied that the true object of it was to lessen expenses, to improve the quality of the coal and to deliver it in the market in the best order to the consumer. These allegations the Court said were immaterial:

Admitting their correctness, it does not follow that these advantages redeem the contract from the obnoxious effects so strikingly presented by the referee. The important fact is that these companies control this immense coal-field; that it is the great source of supply of bituminous coal to the state of New York and large territories westward; that by this contract they control the price of coal in this extensive market, and make it bring sums it would not command if left to the natural laws of trade; that it concerns an article of prime necessity for many uses; that its operation is general in this large region, and affects all who use coal as a fuel; and this is accomplished by a combination of all of the companies engaged in this branch of business in the large region where they operate. The combination is wide in scope, general in its influence, and injurious in effects. These being its features, the contract is against public policy, illegal, and therefore void.

Further commenting upon the agreement, the Court said:

The effects produced on the public interest lead to the consideration of another feature of great weight in determining the illegality of

the contract, to wit: the combination resorted to by these five companies. Singly, each might have suspended deliveries and sales of coal to suit its own interests, and might have raised the price, even though this might have been detrimental to the public interest. There is a certain freedom which must be allowed to every one in the management of his own affairs. When competition is left free, individual error or folly will generally find a correction in the conduct of others; but here is a combination of all the companies operating in the Blossburg and Barclay mining regions and controlling their entire productions. . . . This combination has a power in its confederative form which no individual action can confer. The public interest must succumb to it, for it has left no competition free to correct its baleful influence. When the supply of coal is suspended, the demand for it becomes importunate, and prices must rise. Or if the supply goes forward, the price fixed by the confederates must accompany it. . . . Such a combination is more than a contract; it is an offence. . . . The present case is free of difficulty, the money represented by the bill arising directly upon the contract to be paid by one party to another party to the contract in execution of its terms. The bill itself is therefore tainted by the illegality, and no recovery can be had upon it.

While the courts will not enforce an unlawful agreement or give damages for the non-execution of an unlawful agreement, it does not by any means follow that they will prevent the execution of an agreement which is in reasonable restraint of trade. A good case upon this point is that of the *Bohn Manufacturing Co.* v. *Hollis*.[1] The plaintiff was a manufacturer and vendor of lumber and other building material, a large and valuable part of his trade being with retail lumber dealers. The defendant, the Northwestern Lumbermen's Association, was a voluntary association of retail lumber dealers, formed to protect its members against sales by wholesale dealers and manufacturers to contractors and consumers. The method employed by the association was to demand of every wholesale dealer who sold directly to contractors and consumers 10 per cent of the amount of such sales, and to notify all the retail dealers to refrain from dealing with such wholesale dealer until the payment was made. The plaintiff in this suit, having sold

[1] 54 Minn., 223, decided in 1893.

directly to consumers, was requested to pay the 10 per cent to the association, failing which payment the secretary of the association threatened to send to the other retail dealers the notice provided for in the agreement of the association. Plaintiff demanded an injunction to restrain the issuing of these notices. The Court refused the injunction; it held that the agreement was not in unreasonable restraint of trade or unlawful, and recognized that it was a general rule of trade in every department that wholesale dealers should refrain from selling at retail within the territory from which their customers obtain their business.

What one man may lawfully do singly [says the Court], two or more may lawfully agree to do jointly; the number who unite to do the act cannot change its character from lawful to unlawful. The gist of a private action for the wrongful acts of many is not the combination or conspiracy, but the damage done or threatened to the plaintiff by the acts of the defendant. If the act be unlawful, the combination of many to permit it may aggravate the injury, but cannot change the character of the act. In a few cases there may be some loose remarks apparently to the contrary, but they evidently have their origin in a confused and inaccurate idea of the law of criminal conspiracy, and in failing to distinguish between an unlawful act and a criminal one. It can never be a crime to combine to commit a lawful act, but it may be a crime for several to conspire to commit an unlawful act which, if done by one individual alone, although unlawful, would not be criminal. Hence the fact that the defendants associated themselves to do the act complained of is wholly immaterial in this case.

A somewhat similar case is that of *Cote* v. *Murphy*.[1] In this case, workmen engaged in building trades had combined to advance wages by reducing the hours of labor; and associations of employers in such trades had combined and agreed not to sell materials to contractors who acceded to the demands of the workmen, and to induce other dealers by all lawful means not to furnish such materials. The Court held that such associations of employers were not liable in damages for conspiracy to contractors who, by reason of the combination, were not able to procure all the materials they could dispose of.

[1] 159 Pa. St., 420, decided in 1894.

2. Agreements aiming to raise Prices are Criminal

The early English and American cases, regarding labor as in the nature of a commodity, held very frequently that combinations among workingmen for the purpose of raising wages were, even if unaccompanied by any violence or other unlawful acts, criminal conspiracies. One of the earliest cases in this country was that of *People* v. *Fisher*.[1] In this case, certain journeymen shoemakers had combined for the purpose of fixing the wages of members of the combination. They were indicted under a provision of the New York Revised Statutes which declared that if two or more persons should conspire to commit any act injurious to trade or commerce, they should be deemed guilty of a misdemeanor. This provision is regarded as declaratory of the common law. The Court, in its opinion, declared that a combination to raise wages was injurious to trade or commerce, adding:

> It is important to the best interest of society that the price of labor be left to regulate itself, or rather be limited by the demand for it. Combinations and confederacies to enhance or reduce the prices of labor or of any articles of trade or commerce are injurious. They may be oppressive by compelling the public to give more for an article of necessity or of convenience than it is worth, or, on the other hand, by compelling the labor of the mechanic for less than its value.

It is only fair to say that the Court was influenced in its decision by the fact that the indicted shoemakers left the employment of a master workman, in order to force him to discharge one who had formerly been a member of the shoemakers' association, but who had refused to pay the penalty fixed by the association for violation of the agreement not to work for less than a certain sum. It will be seen, therefore, that in this particular case the conspiracy included not only the combination to raise prices, but also something in the nature of a boycott. The Court remarked:

> In the present case an industrious man was driven out of employment by the unlawful measures pursued by the defendants, and an injury done

[1] 14 Wendell, 9, decided in 1835.

to the community by diminishing the quantity of productive labor and of internal trade. . . . He had a right to work for what he pleased. His employer had a right to employ him for such price as they could agree upon. The interference of the defendants was unlawful; its tendency is not only to individual oppression, but to public inconvenience and embarrassment. I am of the opinion that the offence is indictable.

In commenting upon this general subject of labor combinations, the supreme court of Pennsylvania, in the case of *Cote* v. *Murphy*, already referred to, said:

The fixed theory of courts and legislators . . . was that the price of everything ought to be, and in the absence of combinations, necessarily would be, regulated by supply and demand. The first to deny the justice of this theory and to break away from it was labor; and this was soon followed by . . . legislation . . . relieving workmen of the penalties of what for more than a century had been declared unlawful combinations or conspiracies.[1] Wages, it was argued, should be fixed by the fair proportion labor had contributed in production. The market price determined by supply and demand might or might not be fair wages, often was not, and, as long as workmen were not free by combinations to insist upon their right to fair wages, oppression by capital, or which is the same thing, by their employers, followed. It is not our business to pass on the soundness of the theories which prompt the enactment of statutes. One thing, however, is clear: the moment the legislature relieved one and by far the larger number [*sic*] of the citizens of the commonwealth from the common-law prohibitions against combinations to raise the price of labor, and by a combination the price was raised, down went the foundation on which common-law conspiracy was based, as to that particular subject.

The logical consequence of this change in the law was, in the opinion of the Court, that, after employees had combined to raise wages, any combination made by employers against raising wages was not an unlawful conspiracy, inasmuch as the purpose of the employers was, not to interfere with the price of labor as determined by the common-law theory, but to defend themselves against a demand made altogether regardless of the price as regulated by the supply.

[1] Thus, in New York it is provided that it shall not be a criminal conspiracy for persons to combine for the purpose of advancing or maintaining wages. — Laws of 1870, c. 19.

A perusal of the later decisions upon this subject, sometimes made as a result of a change in the ideas of the judges, sometimes made as a result of specific statutes passed upon the subject, must lead to the conclusion that at the present time a combination of laborers for the purpose of raising wages, if unaccompanied by any unlawful act, — as, for example, a boycott or violence, — is not to be regarded as a criminal conspiracy. One of the latest cases upon the subject is *The Longshore Printing Co.* v. *Howell.*[1] In this case the Court held that it was not unlawful for a union to make provision in its by-laws for a scale of wages, or for limiting the number of apprentices; nor was it unlawful for several or many employees to agree among themselves to quit their employer, in order by so doing to induce him to confine his employment to certain kinds of labor.[2]

But while the law at the present time is that combinations of laborers to raise wages, when unaccompanied by any unlawful acts, are not criminal conspiracies, it cannot be said that the old common law generally has been thus changed. That is, notwithstanding the change made in favor of labor, it is still a crime to combine for the purpose of raising the price of commodities. One of the latest cases decided upon this point is *People* v. *Sheldon.*[3] In this case, certain coal dealers in the city of Lockport entered into an agreement to organize a coal exchange. The object of this exchange was to secure a general supervision and protection of the interests of retail dealers in coal and similar commodities. It was made the duty of members strictly to obey all the provisions of the constitution, by-laws and resolutions of the exchange. Any member guilty of violating any provision of the by-laws, or of conduct unbecoming a member, or of giving short weight or overweight, was liable to forfeit his membership. The agreement further declared that the retail price of coal should as far as practicable

[1] 26 Oregon, 527, decided in 1894.

[2] The common law was the same in the case of a combination of employers to reduce wages. Such a combination was a criminal conspiracy. *Com. ex rel. Chew* v. *Carlisle*, Brightley's Report, Pa., 36.

[3] 139 N. Y., 251, decided in 1893.

be kept uniform; and that no price should be made at any time which should exceed a fair and reasonable advance over wholesale rates, or which should be higher than the current price at Rochester or Buffalo, figured upon corresponding freight tariffs; and that at no time should the price of coal at retail exceed by more than one dollar the wholesale cost, except by the unanimous vote of all the members of the exchange. A certain member of the exchange was indicted, on the ground that this agreement constituted an unlawful conspiracy to increase the price of coal at retail in the city of Lockport, and that in pursuance of it the defendant and other members of the exchange elected officers and by resolution increased the price of coal seventy-five cents per ton. The indictment was found under section 168 of the Penal Code, which is a reënactment of the provision of the Revised Statutes, making it a misdemeanor for any two or more persons to conspire "to commit an act injurious to the public health, to public morals or to trade or commerce." The trial judge submitted the case to the jury upon the proposition that, if the defendants entered into the organization agreement for the purpose of controlling the price of coal and managing the business of the sale of coal so as to prevent competition in price between the members of the exchange, the agreement was illegal; and that if the jury found that this was their intent, and that the price of coal was raised in pursuance of the agreement to effect this object, the crime of conspiracy was established.

The Court of Appeals, in deciding upon the propriety of this charge, said:

The question here does not, we think, turn on the point whether the agreement between the retail dealers in coal did, as a matter of fact, result in injury to the public, or to the community in Lockport. The question is: Was the agreement, in view of what might have been done under it, and the fact that it was an agreement the effect of which was to prevent competition among the coal dealers, one upon which the law affixes the brand of condemnation? It has hitherto been an accepted maxim in political economy that "competition is the life of trade." The courts have acted upon and adopted this maxim in passing upon the validity of agreements the design of which was to prevent competition

in trade, and have held such agreements to be invalid. . . . The organization was a carefully devised scheme to prevent competition in the price of coal among the retail dealers; and the moral and material power of the combination afforded a reasonable guaranty that others would not engage in the business at Lockport except in conformity with the rules of the exchange. . . . The *gravamen* of the offence of conspiracy is the combination. Agreements to prevent competition in trade are in contemplation of law injurious to trade because they are liable to be injuriously used. . . . If agreements and combinations to prevent competition in prices are or may be hurtful to trade, the only sure remedy is to prohibit all agreements of that character. If the validity of such an agreement was made to depend upon actual proof of public prejudice or injury, it would be very difficult in any case to establish the invalidity, although the moral evidence might be very convincing. We are of opinion that the principle upon which the case was submitted to the jury is sanctioned by the decisions in this state, and that the jury were properly instructed that if the purpose of the agreement was to prevent competition in the price of coal between the retail dealers, it was illegal and justified the conviction of the defendant.

Finally, it has been held that corporations may be guilty of the crime of conspiracy, and that they are so guilty when they refuse to sell their products to dealers handling the products of rival companies.[1]

3. "TRUST" AGREEMENTS JUSTIFY FORFEITURE OF CORPORATE CHARTERS

The impossibility, under the existing law, of making contracts in restraint of trade which would be enforced by the courts, and the danger that such agreements would be followed by punishment, led to the formation of agreements which took absolutely out of the power of the original owners of a business all control over it. These agreements, commonly known as trust agreements, provided for trustees who could operate a number

[1] *People* v. *Duke et al.*, *N. Y. Law Journal*, Jan. 23, 1897. It would seem, however, that rebates given on condition that the person receiving the rebate shall deal exclusively with the person giving the rebate are perfectly legal. *Mogul Steamship Co.* v. *McGregor*, H. L. App. Cases, 1892, p. 25; *Nat. Distilling Co.* v. *Cream City Importing Co.*, 86 Wis., 352; *Olmstead* v. *Distilling and Cattle Feeding Co.*, 77 Fed. Rep., 265.

of different enterprises in accordance with their own ideas of what was proper, and who could thus absolutely prevent competition between the parties to the agreements. Such an agreement usually, but not universally, provided for the formation of a corporation out of a partnership wherever a business had been conducted under the latter form. In organizing the trust the stockholders in these corporations exchanged their stock for trust certificates issued by trustees, elected by the persons in interest. The trustees, it was believed, would thus become the only stockholders known to the law, and would therefore have the power of controlling the operations of the corporations whose stockholders had become parties to the trust agreement. In other words, the attempt was made to prevent competition by means of a federation of corporations.

This method was very commonly employed in this country for almost a quarter of a century without being opposed by the public authorities. In 1888, however, attention was directed to a trust agreement in the state of New York, and the attorney-general decided to bring an action in the nature of a *quo warranto* to forfeit the charter of a corporation whose stockholders had participated in its formation. The matter was decided in the case of *People* v. *The North River Sugar Refining Co.*,[1] and this decision was followed by the supreme court of Ohio in *State* v. *Standard Oil Co.*[2] In the New York case the action of the stockholders, even without any formal action upon the part of the corporation, was held to be corporate action, and to be contrary to public policy; the charter of the corporation itself was therefore forfeited. Judge Finch, who delivered the opinion of the Court, said:

I think there may be actual corporate conduct which is not formal corporate action; and where that conduct is directed or produced by the whole body both of officers and stockholders, by every living instrumentality which can possess and wield the corporate franchise, that conduct is of a corporate character, and if illegal and injurious may deserve and receive the penalty of dissolution. . . . The directors of a corporation, its authorized and active agency, may see the stockholders

[1] 121 N.Y., 582, decided in 1890.
[2] 49 Ohio St., 137, decided in 1892.

perverting its normal purposes by handing it over bound and helpless to an irresponsible and foreign authority, and omit all action which they ought to take, offer no resistance, make no protest, but apparently acquiesce as directors in the wrong which as stockholders they have themselves helped to commit. That is corporate conduct, though there may be utter absence of directors' resolutions. . . . The abstract idea of a corporation, the legal entity, the impalpable and intangible creation of human thought, is itself a fiction and has been appropriately described as a figure of speech. It serves very well to designate in our minds the collective action and agency of many individuals as permitted by the law, and the substantial inquiry always is: What, in a given case, has been that collective action and agency? As between the corporation and those with whom it deals, the manner of its exercise usually is material. But as between it and the state the substantial inquiry is only what that collective action and agency has done, and what it has in fact accomplished; what has seemed to be its effective work; what has been its conduct? It ought not to be otherwise. The state gave the franchise, the charter, not to the impalpable, intangible and almost nebulous fiction of our thoughts, but to the corporators, the individuals, the acting and living men, to be used by them, to redound to their benefit, to strengthen their hands and add energy to their capital. If it is taken away, it is taken from them as individuals and corporators, and the legal fiction disappears. The benefit is theirs; the punishment is theirs; and both must attend and depend upon their conduct. And when they all act collectively as an aggregate body without the least exception, and so acting reach results and accomplish purposes clearly corporate in their character, and affecting the vitality, the independence, the utility of the corporation itself, we cannot hesitate to conclude that there has been corporate conduct which the state may review and not be defeated by the assumed innocence of a convenient fiction.

In the Ohio case the reasoning on this head was very similar.[1] In both of these cases, however, the judges felt called upon to consider the further question whether the act which had thus

[1] Judge Marshall said: "The general proposition that a corporation is to be regarded as a legal entity existing separate and apart from the natural persons composing it is not disputed. But that the statement is a mere fiction existing only in idea is well understood and not controverted by any one who pretends to accurate knowledge on the subject. . . . Now, so long as a proper use is made of the fiction that a corporation is an entity apart from its shareholders, it is harmless, and, because convenient, should not be called in question; but where it is urged to an end subversive of its policy, or such is the issue, the fiction must be ignored and the question

taken the form of a corporate act was sufficiently injurious and contrary to public policy to justify the forfeiture of the charter. Here the decisions were somewhat divergent. In New York the Court held that the act of which the corporation had been guilty was in excess of its powers, and that the charter, therefore, was forfeited. The combination of sugar refineries was declared to partake of the nature of a partnership of corporations, and hence to be in violation of law. There was in the opinion a *dictum* as to the injurious effects of monopolies upon the public; but the Court in terms declined

> to advance into the wider discussion over monopolies and competition and restraint of trade, and the problems of political economy. . . . Without either approval or disapproval of the views expressed upon that branch of the case by the courts below, we are enabled to decide that in this state there can be no partnerships of separate and independent corporations, whether directly or indirectly, through the medium of the trust; no substantial consolidations which avoid and disregard the statutory permissions and restraints; but that manufacturing corporations must be and remain several, as they were created, or one under the statute.[1]

In the *dictum* with regard to monopolies, there were several very interesting statements, indicative of the opinion of the Court as to the public policy of permitting combinations whose

determined whether the act in question, though done by shareholders, that is to say, by the persons united in one body, was done simply as individuals and with respect to their individual interests as shareholders, or was done ostensibly as such but, as a matter of fact, to control the corporation and affect the transaction of its business in the same manner as if the act had been clothed with all the formalities of a corporate act. This must be so because, the stockholders having a dual capacity and capable of acting in either, and a possible interest to conceal their character when acting in their corporate capacity, the absence of the formal evidence of the character of the act cannot preclude judicial inquiry on the subject. If it were otherwise, then in one department of the law fraud would enjoy an immunity awarded to it in no other."

[1] The statutes here referred to permitted the consolidation of manufacturing corporations, and the Court in a previous part of the opinion seemed to intimate that a consolidation under the statute would have been perfectly proper, inasmuch as "the resultant combination would itself be a corporation deriving its existence from the state, owing duties and obligations to the state, and subject to the control and supervision of the state, and not [as in the case presented] an unincorporated board, a colossal and gigantic partnership, having no corporate functions and owing no corporate allegiance."

purpose or effect is to promote monopolies. The public interest which corporate grants are always assumed to subserve is most unfavorably affected, said Judge Finch,

when beyond their own several aggregations of capital they compact them all into one combination which stands outside of the ward of the state, which dominates the range of an entire industry and puts upon the market a capital stock proudly defiant of actual values and capable of an unlimited expansion. It is not a sufficient answer to say that similar results may be lawfully accomplished; that an individual having the necessary wealth might have bought all of these refineries, manned them with his own chosen agents, and managed them as a group at his sovereign will; for it is one thing for the state to respect the rights of ownership and protect them out of regard to the business freedom of the citizen, and quite another thing to add to that possibility a further extension of those consequences by creating artificial persons to aid in producing such aggregations. The individuals are few who hold in possession such enormous wealth, and fewer still who peril it all in a manufacturing enterprise; but if corporations can combine and mass their forces in a solid trust or partnership with little added risk to the capital already embarked, without limit to the magnitude of the aggregation, a tempting and easy road is open to enormous combinations vastly exceeding in number and in strength and in their power over industry any possibilities of individual ownership; and the state, by the creation of the artificial persons constituting the elements of the combination and failing to limit and restrain their powers, becomes itself the responsible creator, the voluntary cause of an aggregation of capital which it simply endures in the individual as the product of his free agency. What it may bear is one thing; what it should cause and create is quite another.

In the Ohio case the Court declared the action of the corporations which formed the trust to be void, as contrary to public policy, on the ground that the attempt was made to form a monopoly. The judge said that the object of the agreement

was to establish a virtual monopoly of the business of producing petroleum and of manufacturing, refining and dealing in it and all its products throughout the entire country, and by which it might not merely control the production, but the price, at its pleasure. All such associations are contrary to the policy of our state and void. . . .

Much has been said in favor of the object of the Standard Oil Trust and what it has accomplished. It may be true that it has improved the quality and cheapened the cost of petroleum and its products to the consumer. But such is not one of the usual or general results of a monopoly, and it is the policy of the law to regard not what may, but what usually happens. Experience shows that it is not wise to trust human cupidity where it has the opportunity to aggrandize itself at the expense of others. . . . Monopolies have always been regarded as contrary to the spirit and policy of the law. The objections are stated in "The Case on Monopolies," *Darcy* v. *Allein*, Coke, Pt. XI, 84 b. They are these: (1) "That the price of the same commodity will be raised, for he who has the sole selling of any commodity may well make the price as he pleases"; (2) "The Incident to a monopoly is that after the monopoly is granted, the commodity is not so good and merchantable as it was before, for the patentee, having the sole trade, regards only his private benefit and not the commonwealth"; (3) "It tends to the impoverishment of divers artificers and others who before, by the labor of their hands in their art or trade, had maintained themselves and their families, who will now of necessity be constrained to live in idleness and beggary." The third objection, though frequently overlooked, is none the less important. A society in which a few men are the employers and a great body are merely employees or servants is not the most desirable in a republic; and it should be as much the policy of the laws to multiply the numbers engaged in independent pursuits, or in the profits of production, as to cheapen the price to the consumer. Such policy would tend to an equality of fortunes among its citizens, thought to be so desirable in a republic, and lessen the amount of pauperism and crime. It is true that in the case just cited the monopoly had been created by letters patent; but the objections lie not to the manner in which the monopoly is created. The effect on industrial liberty and the price of commodities will be the same, whether created by patent or by an extensive combination among those engaged in similar industries controlled by one management. By the invariable laws of human nature, competition will be excluded and prices controlled in the interest of those connected with the combination or trust.[1]

[1] A similar decision was made by the supreme court of Nebraska in *State* v. *Nebraska Distilling Co.*, 29 Neb., 700, decided in 1890. See also *Mallory* v. *Hananer Oil Works*, 8 S. W. Rep. (Tenn., 1888), where suit was brought against trustees of a trust agreement by a corporation which was a party to such agreement to recover possession of its property. Judgment was given in favor of the plaintiff on the ground that the corporation could not enter into such an agreement, which the Court considered to be a partnership of corporations.

4. Are Corporations for Purposes of Monopoly Illegal?

The effect of the foregoing and similar decisions was that any persons who intended to form a combination for the purpose of limiting competition were obliged to seek a substitute for the trust agreement. As a general thing they effected an organization in the shape of a large corporation, since, as has been shown, the New York Court of Appeals had appeared to regard this as a legal method of forming a combination. The courts were soon required to decide upon the legality of such action. The first case that came up was that of *People* v. *The Chicago Gas Trust Co.*[1] A gas trust company, as it was called, had been formed, in whose certificate of incorporation the purposes of the corporation were stated to be the manufacture of gas and the purchase, holding and selling of stocks in other gas and electric companies in Chicago or elsewhere in Illinois. *Quo warranto* was brought against the corporation to obtain judgment of ouster against its use of the franchise to purchase and hold or sell the capital stock of other companies. It was clearly admitted on both sides that the Court was not precluded from examining into the legality of the exercise of this franchise by the fact that the certificate of incorporation had been approved and filed with the proper executive officers of the state. The general incorporation act of the state permitted the formation of corporations in the manner provided by it for any lawful purpose. The question which arose was, therefore, whether the corporation in question had been formed for a lawful purpose.

In answering this question the Court found that one result of the exercise of this franchise by the Chicago Gas Trust Company would be that it could control the four other companies in Chicago. The control of these four companies, it was thought, would suppress competition among them, and thus build up a virtual monopoly in the manufacture and sale of gas. The Court said:

Whatever tends to prevent competition between those engaged in a public employment or business impressed with a public character is

[1] 130 Ill., 268, decided in 1889.

opposed to public policy, and therefore unlawful. Whatever tends to create a monopoly is unlawful, as being contrary to public policy.

It therefore held that

if contracts and grants whose tendency is to create monopolies are void at common law, then where a corporation is organized under a general statute, a provision in the declaration of its corporate purposes, the necessary effect of which is the creation of a monopoly, will also be void.

Further on in the opinion it is stated:

To create one corporation for the express purpose of enabling it to control all the corporations engaged in a certain kind of business, and particularly a business of a public character, is not only opposed to the public policy of the state, but is in contravention of the spirit, if not the letter, of the constitution.

The Court also cited with approval the following views expressed by the supreme court of Georgia in the case of *Central Railroad Co.* v. *Collins.*[1]

All experience has shown that large accumulations of property in hands likely to keep it intact for a long period are dangerous to the public weal. Having perpetual succession, any kind of a corporation has peculiar facilities for such accumulations, and most governments have found it necessary to exercise great caution in their grants of corporate powers. Even religious corporations professing, and in the main truly, nothing but the general good, have proven obnoxious to this objection, so that in England it was long ago found necessary to restrict them in their powers of acquiring real estate. Freed as such bodies are from the sure bound to the schemes of individuals, the grave, they are able to add field to field and power to power until they become entirely too strong for that society which is made up of those whose plans are limited by a single life.

For these reasons judgment of ouster was issued against the Chicago Gas Trust Company, as to the exercise of the franchise of purchasing the stocks in other gas companies.

All the cases thus far considered certainly give evidence that the courts of this country regard any combination, whatever form it may take, whose tendency or whose purpose is to form a monopoly, as contrary to public policy and illegal at common

[1] 40 Ga., 582, decided in 1869.

law; but none of them, not even the last, distinctly declares unlawful the formation of a corporation whose purpose or whose effect is to promote monopoly. This question it remained for the supreme court of Illinois to consider in the case of the *Distilling & Cattle Feeding Co.* v. *The People*.[1]

In view of the decisions which the courts were almost universally rendering as to the illegality of trust agreements, the holders of trust certificates in the Distillers' & Cattle Feeders' Trust, commonly called The Whiskey Trust, had in February, 1890, adopted a recommendation of the trustees to form a corporation with a capital stock of $35,000,000. The corporation was thereafter organized. The trustees of the former trust subscribed for all the stock of the new corporation and elected themselves its first directors. They, or so many of them as were necessary to constitute a majority of the directors of each of the corporations composing the trust, also ordered a conveyance of all the property which those corporations held, to the newly formed corporation; and as directors of these corporations, they executed to the Distilling & Cattle Feeding Company a transfer of all of the property of these corporations, and surrendered to the holders of the trust certificates the shares of stock in the newly formed corporation in return for the trust certificates. The new corporation subsequently purchased the property and business of other corporations not parties to the former trust agreement. Suit was brought against the new corporation, and judgment of ouster from its franchise was demanded, on the ground that it had created a monopoly in the manufacture and output of distillery products, and secured such control over the consumers thereof as to destroy all competition in the manufacture and sale of such products throughout the United States.

The Court, in rendering its opinion, said:

There can be no doubt, we think, that the Distillers' & Cattle Feeders' Trust, which preceded the incorporation of the defendant, was an organization which contravened well-established principles of public policy, and that it was therefore illegal. [The new corporation succeeded] to the trust, and its operations are to be carried on in the same way, for the same purposes and by the same agencies as before. The trust then

[1] 156 Ill., 448, decided in 1895.

being repugnant to public policy and illegal, it is impossible to see why the same is not true of the corporation which succeeds to it and takes its place. The control exercised over the distillery business of the country — over production and prices — and the virtual monopoly formerly held by the trust are in no degree changed or relaxed, but the method and purposes of the trust are perpetuated and carried out with the same persistence and vigor as before the organization of the corporation. There is no magic in a corporate organization which can purge the trust scheme of its illegality, and it remains as essentially opposed to the principles of sound public policy as when the trust was in existence. It was illegal before and is illegal still, and for the same reasons.

In answer to the objection that the defendant corporation by its charter was authorized to purchase and own distillery property, and that there was no limit placed upon the amount of property which it might thus acquire, the Court said:

It should be remembered that grants of powers in corporate charters are to be construed strictly, and that what is not clearly given is by implication denied. The defendant is authorized to own such property as is necessary to carry on its distillery business, and no more. Its power to acquire and hold property is limited to that purpose, and it has no power by its charter to enter upon a scheme of getting into its hands and under its control all, or substantially all, the distillery plants and the distillery business of the country, for the purpose of controlling production and prices, of crushing out competition, and of establishing a virtual monopoly in that business. All such purposes are foreign to the powers granted by the charter. Acquisitions of property to such extent and for such purpose do not come within the authority to own the property necessary for the purpose of carrying on a general distillery business. In acquiring distillery properties in the manner and for the purposes shown by the information, the defendant has not only misused and abused the powers granted by its charter, but has usurped and exercised powers not conferred by, but which are wholly foreign to, that instrument. It has thus rendered itself liable to prosecution by the state by *quo warranto*. We are of the opinion that upon the facts shown by the information, the judgment of ouster is clearly warranted.

A case involving somewhat similar questions is that of *The People* v. *The Milk Exchange*, decided by the New York Court of Appeals.[1] The Milk Exchange had ninety-odd stockholders,

[1] 145 N. Y., 267, decided in 1895.

a large majority of whom were milk dealers in the city of New York, or creamery or milk-commission men doing business in that vicinity. At the first meeting of the exchange after its incorporation, the following among other by-laws was adopted: "The board of directors shall have the power to make and fix the standard or market price at which milk shall be purchased by the stockholders of this company." Acting upon this by-law, the board of directors from time to time fixed the price of milk to be paid by dealers, and the prices so fixed largely controlled the market in and about the city of New York.

The court, in deciding the case, declared its conviction that there was a combination on the part of milk dealers and creamery men in and about the city of New York to fix and control the price that they should pay for milk; and that a case was presented in which the jury might have found that the combination referred to was inimical to trade and commerce, and therefore unlawful. Accordingly, the charter was declared forfeited.

It may be claimed [the Court said] that the purpose of the combination was to reduce the price of milk and, it being an article of food, such reduction was not against public policy. But the price was fixed for the benefit of the dealers, and not the consumers, and the logical effect upon the trade of so fixing the price by the combination was to paralyze the production and limit the supply, and thus leave the dealers in a position to control the market, and at their option to enhance the price to be paid by the consumers.

This case is interesting as showing that the courts will take cognizance of an attempt through a combination in the form of a corporation to lower the price of commodities to the detriment of the producer as well as of an attempt to enhance the price at the expense of the consumer.

5. Attitude of the United States Supreme Court

Notwithstanding the decisions thus far considered, persons who desired to form a trade combination were able to do so with impunity, on account of the fact that if their organization was declared illegal in one state, they could organize under the

laws of another, provided the public opinion in the latter was not opposed to trade combinations. An attempt was therefore made in what is known as the Anti-Trust Law, passed by Congress in 1890, to give the national government the power, in addition to that which the states already possessed, to suppress trade combinations. But it was recognized by the promoters of this bill that Congress had no jurisdiction of specifically state industry and commerce. The act was, therefore, worded as follows: "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 one participating in such a contract or engaging in such a combination was declared to be guilty of a misdemeanor, and made liable to severe punishment. It was provided that the circuit courts of the United States should have jurisdiction to restrain violations of the act, and that it should be the duty of the law officers of the United States to institute the proper proceedings. A suit was begun in Pennsylvania against certain sugar-refining corporations which had been absorbed by the American Sugar Refining Company. Evidence was taken before Judge Butler, of the Circuit Court, who said in his opinion: "The object in purchasing the Philadelphia refineries was to obtain a greater influence or more perfect control over the business of refining and selling sugar in this country." The opinion also showed that, after the purchase of these refineries by the American Sugar Refining Company, the latter corporation had obtained control of all refineries in the United States except one in Boston, whose output was about two per cent of the sugar refined in this country.

This case went on appeal to the Supreme Court of the United States.[1] Here, on the state of facts presented by Judge Butler, the Court held that the act of 1890 was framed in the light of well-settled principles; that

Congress did not attempt thereby to assert the power to deal with monopoly directly as such, or to limit and restrict the rights of corporations created by the states or the citizens of the states in the acquisition,

[1] *United States* v. *E. C. Knight Co.*, 156 U. S., 1.

control or disposition of property, or to regulate or prescribe the price or prices at which such property or the products thereof should be sold, or to make criminal the acts of persons in the acquisition and control of property which the states of their residence or creation sanctioned or permitted. . . . The contracts and acts of the defendants related exclusively to the acquisition of the Philadelphia refineries and the business of sugar-refining in Pennsylvania, and bore no direct relation to commerce between the states or with foreign nations. . . . It is true that the bill alleged that the products of these refineries were sold and distributed among the several states, and that all the companies were engaged in trade or commerce with the several states and with foreign nations. But this was no more than to say that trade and commerce served manufacture to fulfil its functions. . . . It does not follow that an attempt to monopolize or the actual monopoly of the manufacture was an attempt, whether executory or consummated, to monopolize commerce, even though in order to dispose of the product the instrumentality of commerce was necessarily invoked. . . . There was nothing in the proofs to indicate any intention to put a restraint upon trade or commerce; and the fact, as we have seen, that trade or commerce might be indirectly affected was not enough to entitle the claimants to a decree. The subject-matter of the sale was shares of manufacturing stock, and the relief sought was the surrender of property which had already passed and the suppression of the alleged monopoly in manufacture by the restoration of the *status quo* before the transfers; yet the act of Congress only authorized the circuit courts to proceed by way of preventing and restraining violations of the act in respect of contracts, combinations or conspiracies in restraint of interstate or international trade or commerce.

It will be noticed that this decision was based upon three grounds: (1) that the proper remedy was not invoked, or at any rate was not invoked at the proper time; (2) that the combination did not disclose an attempt to monopolize; (3) that, even if it did so, it was not a combination in restraint of interstate or foreign commerce.

As to the first of these grounds, it may be said that the bill which was before the court asked that an injunction might issue to prevent and restrain the said defendants from further and continued violations of the act of Congress. This was in addition to the demand that the agreements between the defendants be cancelled and that the shares of stock transferred in perform-

ance of the contracts be restored to their original owners.[1] As to the second ground of the decision, the trial judge found, as has been stated, that the object in purchasing the Philadelphia refineries was to obtain a greater influence or more perfect control over the business of refining and selling sugar in this country. Moreover, the state courts, in the decisions heretofore cited, have declared that they will go back of any alleged purpose of an agreement or of a certificate of incorporation and will inquire what is its real purpose and effect; and that if the latter are to establish a monopoly unreasonably limiting competition, they will declare the agreement void.

But while these first two considerations undoubtedly influenced the Supreme Court somewhat, the main ground upon which the decision was based was that the manufacture and sale of sugar were not interstate or foreign commerce. In order to reach this decision, the Court laid little stress upon the purpose to monopolize the sale. The sale of sugar was declared to be merely an incident to the manufacture. As the Court said, "trade and commerce serve manufacture to fulfil its functions." Laying the weight which they did upon the manufacture, they considered that they were bound by the case of *Kidd* v. *Pearson*.[2] Here the

question was discussed whether the right of a state to enact a statute prohibiting within its limits the manufacture of intoxicating liquors, except for certain purposes, could be overthrown by the fact that the manufacturer intended to export the liquors when made; and it was held that the intent of the manufacturer did not determine the time when the article or product passed from the control of the state and belonged to commerce, and that therefore the prohibitory act was not in conflict with the constitutional provision giving the right to regulate interstate commerce to Congress.

[1] Judge Harlan, in his dissenting opinion, said on this point: "While a decree annulling the contracts under which the combination in question was formed may not in view of the facts disclosed be effectual to accomplish the object of the act of 1890, I perceive no difficulty in the way of the court passing a decree declaring that that combination imposes an unlawful restraint upon trade and commerce among the states and perpetually enjoining it from further prosecuting any business pursuant to the unlawful agreements under which it was formed or by which it was created."

[2] 128 U. S., 1.

Another case which seems to have influenced the Court was that of *Coe* v. *Erroll*.[1] Here the question was "whether certain logs cut at a place in New Hampshire and hauled to a river town for the purpose of transportation to the state of Maine were liable to be taxed like other property in the state of New Hampshire"; and it was held that they were liable to taxation just as much as any other property in the state, and that the owner's intention and his partial preparation to ship them out of the state would not exempt them from taxation as articles of interstate commerce.

Judge Harlan, in a dissenting opinion, pointed out, however, that, under previous decisions of the Supreme Court, interstate commerce embraced something more than the mere physical transportation of articles of property and the vehicles or vessels by which such transportation was effected. He referred in particular to the case of *Mobile County* v. *Kimball*,[2] where it was said that commerce with foreign countries and among the states, strictly considered, consists "in intercourse and traffic, including in these terms navigation and transportation and transit of persons or property, as well as the *purchase, sale and exchange* of commodities." Judge Harlan did not consider that these early statements and decisions had been modified by either of the cases referred to in the majority's opinion. As regards the question of monopoly, he said:

> A combination such as that organized under the name of the American Sugar Refining Company has been uniformly held by the courts of the states to be against public policy and illegal because of its necessary tendency to impose improper restraints upon trade.

And further:

> The object of this combination was to obtain control of the business of making and selling refined sugar throughout the entire country. Those interested in its operations will be satisfied with nothing less than to have the whole population of America pay tribute to them. That object is disclosed upon the very face of the transactions described in the bill, and it is proved — indeed conceded — that that object has been accomplished to the extent that the American Sugar Refining

[1] 116 U. S., 517. [2] 102 U. S., 691.

Company now controls 98 per cent of all the sugar-refining business in the country, and therefore controls the price of that article everywhere. Now the mere existence of a combination having such an object and possessing such extraordinary power is itself under settled principles of law — there being no adjudged case to the contrary in this country — a direct restraint of trade in the article for the control of the sales of which in this country that combination was organized. And that restraint is felt in all the states for the reason known to all, that the article in question goes, was intended to go and must always go into commerce among the several states and into the homes of people in every condition of life.

Finally, Judge Harlan argued for the public policy of the Anti-Trust Law in the following language:

> We have before us the case of a combination which absolutely controls, or may at its discretion control, the price of all refined sugar in this country. Suppose another combination organized for private gain and to control prices should obtain possession of all the large flour mills in the United States; another of all the grain elevators; another of all the oil territory; another of all the salt-producing regions; another of all the cotton-mills; and another of all the great establishments for slaughtering animals and the preparation of meats. What power is competent to protect the people of the United States against such dangers except a national power — one that is capable of exerting its sovereign authority throughout every part of the territory and over all the people of the nation?

The decision of the United States Supreme Court, holding that the manufacture and sale of commodities were not, as not being objects of interstate commerce, subject to the regulation of Congress, was therefore not reached without protest; but the Court was so nearly unanimous in its decision as to justify the belief that the decision itself will not be reversed in the immediate future.[1] The experiences of the states and the arguments advanced by Judge Harlan in his dissenting opinion would lead also to the belief that the regulation of these trade combinations by the states is practically impossible. Any attempt at efficient regulation must come from the national government.

[1] The opinion of the majority in the recent case of the Trans-Missouri Freight Association seems, however, to render the future tendency somewhat uncertain.

In view of the fact that great insistence was laid in the last presidential campaign upon the necessity of some efficient regulation of combinations in restraint of trade, it may be well to summarize the views that the courts have expressed as to the impolicy of permitting these combinations to exist and of recognizing or enforcing in any way contracts for executing their purposes.

The reasons given by the courts for their attitude may be classified under three heads, — economic, social and political. The economic reasons are two in number. In the first place, it is believed by the courts that a combination in restraint of trade and tending to promote a monopoly will result either in the sale of a depreciated article to the public, or in an enhancement of the price of the article which is so controlled. This was the important economic reason at the basis of the decision in the time of Queen Elizabeth, relative to monopolies granted by the crown. This reason has had so much weight with the courts that they have refused to investigate the question whether such has been the effect of a combination. They have simply declared that the possession of monopoly powers by any combination must inevitably result in an enhancement of price or in a depreciation in the quality of the article sold. Their reasoning here, it will be noticed, is distinctly *a priori*; and so long as they adhere to this principle, it will be impossible to prove by reference to actual facts whether it is based upon the truth or not. The second economic argument advanced by the courts in support of their policy is that the fixing by any combination of the price of raw materials injures the producer of the raw material, and will ultimately result in disadvantage to the consumer.

The social argument against combinations also dates from the time of Elizabeth. A monopoly, the Court said,

> tends to the impoverishment of divers artificers and others who before by the labor of their hands in their art or trade have maintained themselves and their families, who will now of necessity be constrained to live in idleness and beggary.

In the form in which it is put, this argument would seem to rest

on a misapprehension of the conditions caused by monopolies; and if applied in as broad a way as it is stated in this case, it would be available against the introduction of all labor-saving machinery. In the Ohio case of *The State* v. *The Standard Oil Co.*, already referred to, this argument was somewhat modified. The Court took the ground, not so much that the formation of the combination throws great numbers of individuals out of employment, as that the development of monopolies transforms great numbers of persons formerly independent into employees or servants. This argument, though treated by the Ohio court as a development of the view of the English court in the case of monopolies, is really quite different in character. A further argument of a social character is to be found in the opinion of Judge Finch in the Sugar Trust case. He based the right of the state to limit the activity of corporations, as distinct from that of individuals, on the ground that a direct grant of corporate powers would, if these powers were not limited, aid in the aggregation of wealth in a few hands. He did not desire to limit the right of individual action, but merely claimed that when specific powers which can only exist as a result of the grant of the state are exercised by individuals, they become rightly subject to regulation in the interest of the state as a whole. It is one thing, said he, for the state to respect the rights of ownership and protect them out of regard to the business freedom of the citizen; but it is quite another thing for the state positively to promote the aggregation of capital by creating artificial persons such as corporations, without limiting their powers.

The political reason advanced by the courts for their position with regard to trade combinations is perhaps as well stated as anywhere by the supreme court of Georgia. Here it is pointed out that all large accumulations of property in hands likely to keep it intact for a long period are dangerous to the public weal. In England it was found necessary to limit the amount of property which even religious corporations might possess, notwithstanding the fact that they, far more than trading bodies, might be expected to exercise their powers for the general good. Given the privilege of legal immortality, corporations, it was held, are apt to "become entirely too strong for that society

which is made up of those whose plans are limited by a single life."

Such are the rules of law in the United States with regard to the legality of trade combinations, and such are the reasons which the courts have advanced for the adoption of these rules. If these reasons are not sound, if the conditions of society are not what they were when these rules were adopted and these reasons were first advanced, it would be well that the rules of law be changed. Changes may be made by legislation, as has very generally been done in the case of labor combinations. If, on the other hand, these reasons are now sound and the rules of law based thereon are at the present time in accordance with public policy, some method ought to be provided for their efficient enforcement. This, it has been pointed out, can in the cases of the largest combinations now in existence be done only through the modification of the present rule of the United States Supreme Court with regard to national regulation of monopolies; or, in case the Supreme Court shall not see fit to modify its rules, by the adoption of a constitutional provision giving the Congress of the United States the necessary powers.

FRANK J. GOODNOW

XV

THE SHERMAN ACT AND ITS INTERPRETATION

AN ACT TO PROTECT TRADE AND COMMERCE AGAINST UNLAWFUL RESTRAINTS AND MONOPOLIES[1]

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

§ 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 a fine not exceeding five thousand dollars, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

§ 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.

§ 3. Every contract, combination in form of trust or otherwise, or conspiracy, in restraint of trade or commerce in any territory of the United States or of the District of Columbia, or in restraint of trade or commerce between any such territory and another, or between any such territory or territories and any state or states or the District of Columbia, or with foreign nations, or between the District of Columbia and any state or states or foreign nations, is hereby declared 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.

[1] 26 Statutes at Large, 209.

§ 4. The several circuit courts of the United States are hereby invested with jurisdiction to prevent and restrain violations of this act; and it shall be the duty of the several district attorneys of the United States, in their respective districts, under the direction of the attorney-general, to institute proceedings in equity to prevent and restrain such violations. Such proceedings may be by way of petition setting forth the case and praying that such violation shall be enjoined or otherwise prohibited. When the parties complained of shall have been duly notified of such petition the court shall proceed, as soon as may be, to the hearing and determination of the case; and pending such petition and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises..

§ 5. Whenever it shall appear to the court before which any proceedings under section four of this act may be pending, that the ends of justice require that other parties should be brought before the court, the court may cause them to be summoned, whether they reside in the district in which the court is held or not; and subpœnas to that end may be served in any district by the marshal thereof.

§ 6. Any property owned under any contract or by any combination, or pursuant to any conspiracy (and being the subject thereof) mentioned in section one of this act, and being in the course of transportation from one state to another, or to a foreign country, shall be forfeited to the United States, and may be seized and condemned by like proceedings as those provided by law for the forfeiture, seizure, and condemnation of property imported into the United States contrary to law.

§ 7. Any person who shall be injured in his business or property by any person or corporation by reason of anything forbidden or declared to be unlawful by this act, may sue therefore in any circuit court of the United States in the district in which the defendant resides or is found, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of the suit, including a reasonable attorney's fee.

§ 8. That the word "person," or "persons," wherever used in this act shall be deemed to include corporations and associations existing under or authorized by the laws of either the United States, the laws of any of the territories, the laws of any state, or the laws of any foreign country.

Approved, July 2, 1890.

No piece of legislation can be understood, much less appreciated, except in the light of the circumstances attending its enactment.[1] This is particularly true of the Sherman Anti-Trust law as applied to transportation. Prior to 1887, industrial combination in the United States had scarcely passed the stage of incubation. Something was evidently doing within; but the outer shell had not yet been broken wide open. Certain combinations, notably the Standard Oil Company, had already, to be sure, grossly outraged public opinion. And it is indubitable that its offenses against commercial decency were among the causes contributing to the passage of the Act to Regulate Commerce in 1887.[2] But the real outbreak of industrial combination over a wider field did not occur for some time thereafter. The later years of the decade of the '80s were associated with active investigation of industrial affairs with the tariff looming large in the background behind the issue of monopoly. A number of anti-trust laws were passed about this period, along with the far-reaching New Jersey statute of 1889, which empowered its corporations to hold stocks in other companies anywhere. It was undoubtedly the public feeling productive of these investigations and bits of state legislation, which also induced Congress to place the Sherman Act upon the statute books in 1890. This statute, succeeding the Act to Regulate Commerce after an interval of three years, seems to have been introduced primarily as a remedy for purely industrial evils, unassociated with railroading as such. For the Interstate Commerce Act was at the time regarded as adequate for dealing with the existing transportation abuses.

The Congressional history of the Sherman Act is important in its bearings upon the question as to the intent to bring common carriers within the prohibitions of the statute.[3] As early as 1888 Senator Sherman of Ohio introduced a bill declaring all combinations, conspiracies and agreements in restraint of trade

[1] From W. Z. Ripley, Railroads: Finance and Organization, pp. 549–574.

[2] Ripley, Railroads: Rates and Regulation, p. 445.

[3] Most conveniently traceable in Bills and Debates in Congress Relating to Trusts, 57th Cong., 2d sess., Senate Doc. no. 157, I, 1903; Autobiography, by Hon. G. F. Hoar, vol. II, p. 362 *et seq.*

unlawful. This died in committee. An identical bill, except for the elimination of "conspiracy" and "restraint of trade" was reintroduced in the following year. The first decisive step was taken in 1890, when the Committee on Judiciary reported to the Senate, recommending that everything except the enacting clause in the latest Sherman bill should be stricken out, and that an entirely new measure drafted by Senator Hoar of Massachusetts be substituted.[1] It was this bill which subsequently became the Sherman Act, so called as Senator Hoar somewhat tartly observes "only because Sherman had nothing whatever to do with it."

It is uncertain whether it was originally intended to include railroads under the Anti-Trust law. The indetermination of the Congressional mind is clearly brought out in the divided opinion of the Supreme Court of the United States in the Trans-Missouri Freight Association case.[2] Five justices declared that it was "impossible to say what were the views of a majority of the members of each house," as well as "that the debates in Congress are not appropriate sources of information for this purpose." Not satisfied with this disposition of the matter, four justices in the dissenting opinion reviewed in detail the Congressional history of the bill. Evidence was found to their satisfaction that a determined effort was made, by means of amendments proposed, to include transportation contracts or agreements, but that the effort was unsuccessful. According to this interpretation there was no purpose to interfere with the Interstate Commerce Act. These dissidents, consequently, held that all activities of common carriers should be adjudged according to the provisions of the Act to Regulate Commerce of 1887 and not by the Sherman Act at all. It is rather significant in view of this closely divided opinion, that the statute has subsequently been so broadly applied to the common carriers of the country in the series of decisions henceforward to be reviewed.

The text of the Sherman Act[3] "To protect trade and com-

[1] 21 Cong. Record, pp. 2901 and 4089.
[2] 166 U.S. 317 and 359.
[3] Reprinted in full, pp. 484, *supra*.

merce against unlawful restraints and monopolies" in the first section declares illegal:

> 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.

The second section turns from restraint of trade to monopoly.

> 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,

commits a misdemeanor, punishable by fine and imprisonment. By the third section of the Act, the same prohibitions are made applicable to the territories as well as to the states. The remaining clauses are unimportant for our purpose save, perhaps, the sixth which declares any prescribed property in the course of interstate transportation forfeit and defines the word "person" as including corporations. The law was indeed quite brief by comparison with the extended and elaborate Interstate Commerce Act.

As a background for the examination of the application of the Sherman Act to railroads, attention should be directed to the extreme unevenness with which that statute has been enforced by Federal executive authority. Only thus does it become apparent why combination among railroads was enabled to attain so considerable a momentum before the inhibitions of the Act were brought into play at all. The record of the different presidential administrations is illuminating. As Professor Seager observes,[1] it will now scarcely be denied that three successive presidents and five successive attorneys-general were seriously remiss in their duty. Under the administration of President Harrison, to March, 1893, only four bills in equity were filed, and but three indictments were returned. The succeeding term of President Cleveland, to 1897, witnessed the same number of bills with only two indictments. The disappointing

[1] *Political Science Quarterly*, vol. XXVI, 1911, p. 584. The pamphlet summary of Anti-Trust Decisions, published by the Department of Justice annually, contains the record.

outcome of the first prosecutions attempted probably accounts in a measure for this lack of interest; although the affirmed illegality of railroad pooling somewhat relieved the monotony. The low water mark of enforcement of the Anti-Trust law was touched under President McKinley, during the four years 1897–1901. The statute was practically a dead letter so far as either railroads or industrial combinations were concerned. The artillery of the Department of Justice was, to be sure, trained upon one petty live stock combination and certain agreements among local coal dealers. But the attention of the country seems to have been fixed rather upon sowing the seeds of monopoly than upon any attempt to prepare the soil for a more healthy industrial crop.

During this long dull period, while the existence of "teeth" in the Sherman Act was so wholly unsuspected, it is not surprising that its judicial interpretation as applied to railroads occurred only in connection with pooling. As a matter of fact the great railroad combination movement did not get under way until somewhat later. Hence the distinction of applying almost the first test was reserved for the Trans-Missouri Freight Association in 1897.[1] The structure and functioning of organizations of this sort will be considered in the next chapter; but, inasmuch as this first railroad decision really turned upon the question of monopoly rather than of pooling *per se* as defined in the Act of 1887, its legality may be considered as a thing quite separate and apart from its economic serviceableness. This is particularly true since the latest turn of interpretation, awaiting our analysis, which holds that legality is to be adjudged in the light of reason and not according to any absolute and arbitrary standard. As for the Trans-Missouri Freight Association proceedings, both of the lower Federal courts held that the Sherman Act had not been violated; and the Supreme Court decision, reversing these judgments, was, as we have already seen, rendered by a bare majority, four justices out of nine dissenting. The first aspect of the matter, namely as to whether the Anti-Trust law comprehended common carriers by rail, has

[1] 166 U. S. 290; reprinted as 55th Cong., 1st sess., Senate Doc. no. 12; *cf.* also *Harvard Law Review*, Vol. XI, 1897, pp. 80–94.

already been touched upon; especially the strong dissenting view that in the absence of a definite application of the Anti-Trust law to railroads, inasmuch as the statute was expressed in general terms while the Act to Regulate Commerce antedating it by three years was specific, the latter exempted the carriers entirely from the drastic prohibitions against monopolistic combination.

The second judicial construction of the Sherman Act for common carriers within a few months reënforced the first. The Joint Traffic Association, an agreement entered into in 1895 by thirty-two railroads operating east of Chicago, was declared unlawful in 1898.[1] This pool was attacked not only as violating the Anti-Trust law, as in the Trans-Missouri case, but also as being contrary to the Act to Regulate Commerce. An attempt was made to distinguish between this and the Trans-Missouri Freight Association case, on the ground that the latter association actually conferred power to fix rates, whereas the Joint Traffic Association merely provided for the adoption jointly of such rates as were in force. Both of the lower Federal courts once more held that such agreements were not repugnant to the provisions of the Interstate Commerce Act. But the force of the argument in the Supreme Court was directed entirely to the interpretation of the Anti-Trust law; and it was finally decided, as in the preceding case, that the agreement was in contravention of that statute.

Between the pooling decisions in 1897 and the suggested reorganization of the St. Louis Terminal Company fifteen years thereafter, despite the extraordinary activity in the field of railroad consolidation described in the preceding chapters, the Supreme Court only once passed upon the validity of attempts to substitute monopoly for competition in railroading. The one interrupting opinion is of great importance; but, before proceeding to its examination, it may not be out of place to inquire still further as to the reasons for the prolonged judicial quiescence. It is the more striking in view of the new life infused into the Sherman Act under the administration of President Roosevelt in 1901–1909. No fewer than twenty-five indictments and

[1] 171 U. S. 505.

eighteen bills in equity were returned, by way of contrast with only five indictments and ten bills in equity during the entire three preceding presidential terms. But even greater assiduity was to characterize the administration of President Taft to 1913. Within a period scarcely half the length of Roosevelt's term, twenty indictments and seventeen bills attended the vigorous initiative of the Federal Department of Justice. Quite apparently it was only after the more impressive and convincing manifestations of the evil of monopoly in trade and manufacture had been disposed of, that the attorney-general was able to redirect attention to the common carriers. It is probable, also, that the Northern Securities decision, which alone broke the long period of immunity from prosecution of the railroads, was in itself of such compelling importance that much was accomplished informally in the way of admonition and repression. The fact also deserves consideration that the peculiar interpretation placed upon the Sherman Act by President Roosevelt, inducing him to stay the original proceedings instituted in 1908 against the New Haven combination, undoubtedly operated to discourage a more searching test of the law as applied to common carriers at the time.

Narrowly viewed, the Northern Securities decision in 1904[1] is significant as abruptly putting an end to the holding company as a legal instrumentality for the attainment of monopoly, and as coincidently displaying cautionary signals with regard to the possible misuse of intercorporate stock ownership. The facts in the case have already been spread upon our pages in various other connections and do not call for restatement. The condemnation was explicit. "If Congress has not, by the words used in the (Sherman) Act, described this and like cases, it would, we apprehend, be impossible to find words that would describe them." For without such judicial construction "then the efforts of the national government to preserve to the people the benefits of free competition among carriers engaged in interstate commerce will be wholly unavailing, and all transcontinental lines, indeed the entire railway systems of the country,

[1] 193 U. S. 197. The material facts are given *in extenso* in Ripley, Railroads: Finance and Organization, and Railway Problems, rev. ed., chapter XXI.

may be absorbed, merged and consolidated, thus placing the public at the absolute mercy of the holding corporation." The objection was swept aside that the prohibition of unrestricted intercorporate stockholding would be an unconstitutional infringement upon the right to do as one wills with one's property. The immediate and direct result of the decision, then, was to relegate the holding company along with the "trust" to harmless disuse. But the importance of the Northern Securities opinion does not stop here. It is even more commanding upon broad constitutional grounds. Two separate questions were treated and settled at one and the same time. The first appertained to the competing and conflicting powers of the different states with one another. The second confronted the sovereignty of the several states with that of the Federal government. It was the mere ownership by one corporation of the capital stock of another which started the trouble, to be sure; but from this kernel the controversy grew and spread until the ultimate principles of our framework of government became involved.

As to the conflicting authority of state with state, in the matter of railroad stockholdings, our preceding review of the material facts is almost self-explanatory. The state of New Jersey through its license by charter to the Northern Securities Company to hold railway stocks without let or hindrance, except for the obligation to pay taxes into the state treasury, empowered it to commit acts within the jurisdiction of a sister state which were repugnant to the laws thereof — as well as to the Federal Anti-Trust law, after which most of the state statutes were fashioned. For, in consequence of the deeply aroused public opinion throughout the Northwest, the Northern Securities Company had already been put to the test, as well in the highest state courts as in the Supreme Court of the United States, under the provisions of the Anti-Trust law of Minnesota; and the device of the holding company had thus been found to be in contravention of the terms and intent of that state statute.[1] Any state, as the opinion ran, did it so choose, might submit to the existence of combination within its own limits that restrained its internal trade; but beyond that frontier it might not "project

[1] *Pearsall* v. *Great Northern*, etc., 161 U. S. 646.

its authority into other states and across the continent." No longer could immunity by a New Jersey corporation be successfully maintained within the territory of Minnesota against the expressed will of the people of that commonwealth. The soundness of this general rule is above dispute.

Equally plain was the purport of the Northern Securities decision in its affirmation of the paramount authority of the Federal government over the several states; even in such matters of seemingly private finance as the charter right to hold stocks in their own corporations. Much depended at this point upon the nature of stock ownership, that is to say, as to whether interstate stock ownership was in reality interstate commerce. No difference of opinion is evident upon the proposal that Congress should stay its hands "to the detriment of the public because, forsooth, the corporations concerned or some of them are state corporations. . . . No such view can be entertained for a moment." But serious dissent was registered against the affirmation that stock ownership and interstate commerce were indistinguishable at law. Yet, notwithstanding the vigorous dissenting view that Congress was void of power to regulate or control the acquisition and ownership of railway stocks by the Northern Securities Company, the majority opinion to the contrary prevailed, and thus became law.

Peculiar significance in a large way also attaches to the Northern Securities decision as foreshadowing an about-face on the part of the Supreme Court in the general interpretation of the Sherman Act. Perhaps the most puzzling feature of this brief and seemingly drastic statute, as judicially construed, presents itself in this connection. Are all arrangements or practices without exception or limitation of any sort forbidden; or was it the intention merely to prohibit those which potentially or actually were unreasonable? Is competition to be perpetuated regardless of results; or shall a sound public policy permit a distinction between those acts provocative of economy and efficiency and those others which are necessarily and always inimical to the common welfare? Throughout the extended series of decisions applying the Anti-Trust law under all sorts of circum-

stances and conditions, the notable change in opinion is, oddly enough, in view of the fact that this statute was originally intended to deal with business rather than transportation, most clearly discernible in the great railroad cases. As we have already seen, in the test applied in the pooling cases in 1897–1898, the Court by a bare majority held that the statute forbade all combinations of whatever sort, reasonable and unreasonable alike.[1]

In the Northern Securities case, the majority of the Court after the lapse of seven years still adhered to its original construction as to reasonableness; but Justice Brewer, in what is possibly the most significant portion of the entire decision, announced his conversion to the belief that the ruling, not only in this but in the pooling cases as well, should have condemned the arrangements at bar because they were restraints upon trade which were unreasonable *per se*, and not merely because they operated to interfere somehow or other with the free exercise of competition. The dissenting opinion of Justice Holmes also coincided with this view of the matter. The prohibitions of the law "certainly do not require all existing competitions to be kept on foot. . . . I am happy to know that only a minority of my brethren adopt an interpretation of the law which in my opinion would make eternal the *bellum omnium contra omnes* and disintegrate society so far as it could into individual atoms. If that were its intent I should regard calling such a law a regulation of commerce as a mere pretence. It would be an attempt to reconstruct society." It only remained for the conversion of the remaining justices to take place in the next great case. Out of the confusing fogs of legal doctrine and the disturbed cross currents of interpretation of economic history, the Supreme Court at last emerged upon the broad and open sea in the great Standard Oil Company decision of 1911.[2] Dissent

[1] This development is most clearly traceable in the Standard Oil opinion of 1911, page 552, *infra*, to which should be added the concurring opinion of Justice Brewer in the Northern Securities case, 193 U. S. 361; and the dissenting opinion, *idem*, 407 ff. *Cf.* Young's dissents from this view in *Journal of Political Economy*, vol. XXIII, 1915, p. 205.

[2] 221 U. S. 1.

almost vanished. With substantial unanimity it was held unequivocally that the Anti-Trust Act was to be construed "in the light of reason." All but one member of the Court agreed that the prohibition applied only to such contracts and combinations as amounted to an unreasonable or undue restraint. All other arrangements which conduced to a smoother and more efficient conduct of business were declared lawful.

Merely to prove monopolistic intent or attainment, irrespective of its nature or quality, under all the complicated circumstances of modern industrial life, is at best a difficult task. But it is far easier than to attempt to draw the line between "good" and "bad" restraint, actual or potential. Yet such was the obligation imposed upon itself by the Supreme Court through its new construction of the statute. The first occasion in the field of transportation was offered in complaint against the St. Louis Terminal Railroad Association. The opinion [1] clearly exhibits the advantages which may be expected to flow from an interpretation of the Anti-Trust law according to the rule of reason laid down in the Standard Oil case. For the first time one might entertain hope of constructive results to flow from the differentiation of concerted acts inimical to the public interest, from those which, rightly applied, would contribute to the public advantage. The facts were as follows: Although twenty-four railroad lines converged at St. Louis, not a single one passed through the city. About one half of them terminated on the east bank of the river, which, once the location of a great trade by water, had now become an obstacle in the way of free intercourse by rail. The volume of traffic at this point was enormous. It was impracticable that each separate road should have its own Mississippi bridge. The cost was prohibitive. And ample facilities could be provided, as in fact they were, only by associated action. Besides the river as an obstacle to passage, the location of the city upon hills approaching close to the river bank, made it impossible to enter the municipal limits by rail from the west except along certain well-defined approaches. In order to cope with these physical obstacles at St. Louis, two separate bridge corporations and a ferry line cared for the necessary passage

[1] 224 U. S. 383; decided April 22, 1912.

over the Mississippi; while certain other transfer and terminal companies came into being in order to provide the necessary connections into town. All of these instrumentalities in the course of time were taken over by the Terminal Railroad Association, organized in 1889. This corporation, in turn, was not independent. It was itself controlled by a nicely balanced and evenly divided stock ownership among fifteen trunk lines. The cause of complaint was the alleged inability of remaining carriers, notably the Rock Island, to obtain the most-favored-nation treatment as to rates and facilities. Admission by newcomers was rendered difficult by the charter requirement of a unanimous consent of the associated lines. It was complained that this entire arrangement was inviolation of the Anti-Trust law, and in its effect was contrary to the public interest.

The Supreme Court found that the St. Louis Terminal company was in violation of the law; and undoubtedly under the earlier interpretation of the statute, as applied in the pooling cases, matters would necessarily have rested at that point. No alternative but dissolution would have remained. But a great advance is marked in the added qualification that "the violation of the statute grows out of administrative conditions which may be eliminated and the obvious advantage of unification preserved," in such a manner "as will amply vindicate the wise purpose of the statute and will preserve to the public a system of great public advantage. In other words, the Supreme Court of the United States, noting the economic waste and the expense and inconvenience to the public which would result from a disruption of this coöperative arrangement, tempered its findings in such a way as to make the decision in reality a victory at once for the terminal association, the railways and the people. Certain modifications of organization and practice were prescribed, as conditions necessary for the continued lawfulness of the terminal association. Among these requirements was one calling for the admission of any existing or future railways to joint ownership and control; another extended the facilities of the terminals under reasonable terms to any carriers not electing to become joint owners in the association; and a third abrogated the existing restriction of the proprietary companies to the use

of the terminal companies' lines. Over and above these, the Supreme Court called for the discontinuance of certain practices of charging an "arbitrary" for trans-Mississippi traffic originating within one hundred miles. These conditions, however, are merely matters of detail. Considerable dispute ensued as to particulars. For our purposes they simply serve to illustrate the manner in which a penetrating discernment may reconcile the financial and operating necessities of the railroads with the interest of the public, in the perpetuation of such competition in service as shall make for efficiency.

Appraised both by the financial magnitude and the geographical extent of the interests concerned, the proceedings to bring about the dissolution of the Union Pacific-Southern Pacific merger probably outrank any other test likely to be applied to railroads under the Sherman Act. This combination stood for monopoly to the third power. It was the logical climax of a tendency, stayed at its height by the stern hand of the law. A repetition of the facts is unnecessary in view of their extended statement heretofore. Official proceedings began with the original report of the Interstate Commerce Commission in 1906. The dissolution suit, prosecuted for five years, resulted unexpectedly enough in an opinion by the Circuit Court unqualifiedly adverse to the government. Two justices held that the Union Pacific and the Southern Pacific were connecting and only incidentally competing lines. The third judge dissented from this view. The case then went on appeal to the Supreme Court. The final opinion,[1] considering the voluminous record, was surprisingly brief. Nor did it differ from other recent pronouncements, in confining attention largely to economic fact in preference to legal doctrine. For the occasion called merely for the application of predetermined law to an elaborate set of material circumstances. Three questions called for answer. (1) Was there competition between the constituent railroads in the Harriman system prior to its formation? (2) Did the merger eliminate such competition, assuming that it had existed? (3) If there had been competition, and it had ceased, was its suppression brought

[1] 226 U. S. 61; decided Dec. 2, 1912.

about by unlawful means? An affirmative answer to these three queries was essential to the government's success.[1]

A notable feature of the Union Pacific dissolution, which marks a distinct advance over its predecessors, was the care bestowed upon the segregation of the great properties concerned. The government had not been altogether successful in its mandates heretofore. The Northern Securities dissolution was merely formal.[2] The Standard Oil proceedings were entirely farcical. Some improvement marks the Tobacco Trust segregation, inasmuch as its complex organization forbade so naïve a decree in relief. The remedy prescribed in the St. Louis Terminal case was for the first time really constructive. The delicacy of adjustment requisite in the Union Pacific affair is exhibited by the complications which attended the various plans worked out in this instance. There were no less than four of these.[3]

The first dissolution plan proposed to distribute the Union Pacific's entire holdings of 1,266,500 shares of Southern Pacific common stock among its own shareholders *gratis*. This was vetoed by the Supreme Court, on the very proper ground that it would leave control in exactly the same hands as before, except that such control would be exercised through the medium of private persons, — dominant stockholders of the Union Pacific.[4] This was precisely what happened with the Standard Oil Company. The second plan likewise came to grief. It proposed: first, a sale of Southern Pacific stock, under privileged conditions, to all shareholders *both* of the Union Pacific and Southern Pacific companies, except, of course, to the Union Pacific corporation or the Oregon Short Line company; and, secondly, with funds thus acquired, an outright purchase by the Union Pacific from the Southern Pacific of the Central Pacific link. A number of obstacles speedily developed. Conflicting stipulations in the indenture of bond issues stood in the

[1] These details are admirably reviewed by Daggett in the *Quarterly Journal of Economics*, vol. XXVII, 1913, pp. 295–328, reprinted in our Railway Problems (rev. ed.), chapter XXII.

[2] Condemned by the dissenting opinion, 193 U. S. 373.

[3] *Quarterly Journal of Economics*, vol. XXVIII, 1914, pp. 772–794.

[4] 226 U. S. 470.

way. An almost hopeless physical entanglement of the two properties had grown up in the course of time. Thus, on San Francisco bay one company owned the piers, another the approaches and a third the ferry. But the greatest objection came from the aroused public sentiment of California, which through its railroad commission insisted upon the continuance of actual competition at all points. Thus the advantage of this plan to the Union Pacific, in that it would give the long-desired access over its own rails to the coast — its alleged motive for originally taking over the Southern Pacific, be it remembered — was denied.

A third scheme was then evolved, quite different in principle. All the Southern Pacific shares were to be distributed *pro rata* among the Union Pacific stockholders, as by the first plan, but such disposition was to be coupled with disfranchisement for all purposes of control, of all holders of 1000 shares or over. A trustee was to issue certificates of interest upon deposit of all Southern Pacific shares held by the Union Pacific, which were to carry no voting rights while so held, and which should be exchangeable for actual Southern Pacific shares only on affidavit that the applicant for exchange held less than 1000 shares. This plan would exclude 368 selected private shareholders from further increase of their holdings, and would thus appear to have been of doubtful legality.

The final plan adopted in July was entirely different in many ways. It aimed to dissolve another similar control by the Pennsylvania Railroad of a competing line, by substituting in each case control or at least a dominant interest in merely a connecting line. The Pennsylvania exchanged 212,737 preferred shares at $80 and 212,736 common shares at par of the Baltimore & Ohio Railroad with the Union Pacific system for its 382,924 shares of the Southern Pacific at par. This left the Union Pacific with a balance of 883,576 shares of Southern Pacific stock, which balance it was authorized by the Court to distribute to the extent of 27 per cent of their then holdings among the other general shareholders of its own company. The expedient of issuance of certificates of interest by a trustee to be exchanged for actual stock upon affidavit that purchase

was made in good faith on his own behalf, independently of the Union Pacific interests, was borrowed from the preceding plan. The price of such privileged subscription was made so favorable that the certificates when offered were subscribed for two and one-half times over. The final step was the distribution of the Baltimore & Ohio stock as a dividend to Union Pacific shareholders. Disregarding details, this amounted to about $89,000,000, the greater part of which was the profit made by fortunate investments in railroads elsewhere.[1] This last plan, it will be observed, differed from the first two, in that it left the Central Pacific link to the coast still in the hands of the Southern Pacific. But this feature, held by the outgoing Administration as essential, was not emphasized by the new Democratic attorney-general; and as for the Union Pacific, it was deemed that a traffic alliance with the Central Pacific providing for a through route and most-favored treatment as to facilities for interchange — guaranteed in any event by the significant clause upon the subject in the Hepburn law of 1906 — would in some ways be preferable to ownership. It would be more elastic and would, moreover, as a detail of interstate commerce, be free from interference by the railroad commissions of the states concerned. Such a traffic agreement would also insure to the Union Pacific a due share of east-bound business, which otherwise, had it purchased the Central Pacific, the Southern Pacific might choose to route entirely over its own long line. Thus was the dissolution brought at last to a successful termination.

The arrangement resulting from the dissolution of the Harriman system, as ultimately put through, was defective in its failure to fulfill the original intention of Congress to encourage by liberal land grants and subsidies the construction of the first transcontinental railroad. For by the acts of 1862–1864 it was provided that "the whole line of said railroad . . . shall be operated and used for all purposes of communication . . . so far as the public and Government are concerned, as *one connected continuous line*." (Our italics.) So long as the Central Pacific link remained in the hands of the Southern

[1] Ripley, Railroads: Finance and Organization, chap. XV.

Pacific, therefore, the primary purpose of this historic legislation was thwarted. Reconsideration and conviction upon this point led to the institution of another suit in 1914 by the Department of Justice, this time to compel the Southern Pacific to terminate its control of the Central Pacific.[1] The logic and facts of the situation reënforced the contention of the government that the public interest, particularly of the Pacific slope, would be promoted by this means. Competition in transportation with the outside world is and has always been the supreme need of California. Yet, as we have already seen, so long as the Southern Pacific owned a continuous water and rail transcontinental line, the entire earnings of which it retained without pro-rating division, whereas on all traffic by the alternative direct route over the Central Pacific it must be contented with but a fraction of the joint through rate, just so long was it bound to encourage the southern or Sunset Route at the expense of the other. For many years, to be sure, it exchanged much business with the Union Pacific, being impelled thereto by the desire to secure reciprocal advantages; but the record in the original Harriman dissolution proceedings contains much evidence of a denial of the equal advantages and facilities called for by the Act of 1864 and even of actual discrimination against its own link in the direct route to the East.

Were the Central Pacific to be set free, as pointed out in the government's petition, it might also, by recourse to but little new construction, create a truly competitive line between San Francisco and Portland, Oregon. Yet once again the pending attempt of the government to secure for the Pacific slope the great commercial advantage of "one connected continuous line" was opposed by certain California shippers. They predicted that the loss of the Central Pacific would so weaken the Sunset Route as to unfit it for effective competition in future. In gaining a better direct line they feared crippling the roundabout one. The advent of the Panama Canal naturally had to be reckoned with. In the past the Southern Pacific had undoubtedly been restrained somewhat from whole-hearted competition with the all-water lines, lest it might prejudice thereby

[1] Original Petition, *U. S.* v. *So. Pac.;* U. S. Dist. Court, Utah, etc.

its considerable investment in the direct route *via* Ogden. Nevertheless, were this investment to be closed out, was it not equally possible that more, rather than less, vigorous efforts might be made to tempt traffic from the sea routes to the all-rail line? All things considered, both domestic and Oriental business alike, it would appear as if the probable splitting up of the Southern Pacific monopoly, followed perhaps by closer relations between the two connecting railroads which meet at Ogden, might bring to pass at last, after the lapse of half a century, a direct connected continuous line between East and West which would more closely bind California to the rest of the United States.

Close upon the heels of the decree calling for the dissolution of the Harriman system followed the opinion of the Supreme Court with reference to the so-called Anthracite Coal Trust.[1] As to the charge that a general combination existed, the Court held unanimously that the case was "barren of documentary evidence of solidarity." The Court declined, in other words, to base an opinion upon inference which, as it would appear, was sufficiently plain; but it insisted upon the proof of specific acts or transactions in pursuance of monopolistic intent. Yet the conclusion of the protracted suits was not entirely disappointing. For a second time did the holding company come under the ban of the law. The Temple Iron Company was adjudged to be an unlawful combination, whereby an independent railroad had been "strangled." The Court also directed a cancellation of all of the so-called percentage contracts, by means of which the allied coal roads had sought to tie the hands of independent producers in perpetuity. No opinion was expressed regarding the legality of the control of the Central of New Jersey by the Reading, or of various other similar transactions.[2] Some advance was undoubtedly made in the direction of liberating the people of the United States from unjust extortion; and the institution of additional suits,

[1] 226 U. S. 324; decided Jan. 16, 1912. Eliot Jones, *op. cit.*, p. 212 *et seq.*, outlines the course of this litigation.

[2] On Oct. 28, 1915, the Central of New Jersey was ordered to dispose of its coal properties.

still pending, holds out the hope that more may yet be accomplished in due time. Whether or not the existing informal understanding, based upon the mutual self-interest of the great coal roads concerned, may serve as effectively as formal or contractual arrangements, which are clearly ruled out, may not yet be predicted with certainty. A satisfactory solution of the anthracite coal problem is by no means yet in sight.

A step in the right direction, nevertheless, is taken in a recent decision of the Supreme Court,[1] which in the case of the Lackawanna railroad, holds the exclusive contract by which the carrier and the coal sales company, which it set off from itself in 1909, to be in violation both of the Commodities Clause [2] and the Anti-Trust law. The railroad was consequently enjoined from transporting coal, which it had sold to the sales company. What the outcome will be, remains yet to be seen.

Our record as to railroads under the Sherman Act concludes with the dissolution of the great New England transportation monopoly. The best evidence that this statute is now recognized as a vital piece of legislation is afforded by the fact that in this instance protracted and expensive suits were avoided by a dissolution agreement, reached in conference between the New Haven and the Federal Department of Justice. Strong pressure undoubtedly was brought to bear. And the company yielded, not because the illegality of its combination was conceded, but only because it was feared that prolonged litigation might precipitate a receivership. It will be recalled that in 1908 the Roosevelt administration had instituted proceedings, which were afterward discontinued by a formal agreement between the President and the New Haven management that the latter would thereafter be a "good" monopoly. How faithfully this promise was kept has already been recited. A second bill of complaint praying for dissolution brought matters to a head in 1914, only to be withdrawn upon a formal agreement providing for the resolution of the system into its component parts.

[1] June 21, 1915; 35 Supreme Court Rep. 873.

[2] Ripley, Railroads: Rates and Regulation, pp. 513 and 552.

The dissolution plan was officially summarized as follows:

First. The Boston Railroad Holding Company is a Massachusetts corporation holding a majority of the stock of the Boston & Maine Railroad, and 90 per cent of the former's stock in turn is owned by the New Haven railroad. The charter of the holding company prohibits it from disposing of the Boston & Maine stock. The legislature of Massachusetts will be asked to remove this prohibition, and if this is done the stock of the holding company will be transferred at once to five trustees, and, after arrangements have been made to protect the minority stock of the holding company, they shall sell the Boston & Maine stock prior to January 1, 1917.

Second. The stocks of the companies which control the Connecticut and Rhode Island trolleys will be placed in the hands of trustees — five for each state — and shall be sold within five years from July 1, 1914.

Third. The majority stock of the Merchants & Miners Transportation Company, now held by the New Haven, will be placed in the hands of three trustees and shall be sold within three years from July 1, 1914.

Fourth. The minority stock in the Eastern Steamship Corporation, held by the New Haven, shall be sold within three years from July 1, 1914, and in the meantime shall be deprived of voting power.

Fifth. Whether the New Haven Railroad shall be permitted to retain the sound lines will be submitted to the Interstate Commerce Commission for determination under the provisions of the Panama Canal act.

Sixth. The Berkshire trolleys shall be sold within five years from July 1, 1914.

The financial magnitude of this operation is exhibited by the following table of the book value of the various investments of the New Haven system. The principal lesson to be deduced from this case is the force of public opinion acting through law to bring a once insolent and corruptly powerful corporation under restraint. The obligation henceforth rests upon the people to exercise this power constructively in the interest of all parties concerned. It is by no means certain that all, or even many, of the units in the New Haven system were really competing rather than merely supplementary lines; still less that the welfare of New England will be promoted by a rigid insistence

upon corporate disruption. Could the matter have been brought to a test as to its legality, as would surely have happened under more auspicious financial circumstances, some very pretty transportation problems would have come to light.

	As Carried on Books of	
	New Haven Company	New England Navigation Company
Boston Railroad Holding Company	$29,371,165.97	
Boston & Maine R.R. subsidiary lines	1,417,216.95	
The Connecticut Company	2,125,000.00	$40,000,000.00
The Rhode Island Company	27,852,336.41	1,266,379.37
Berkshire Street Railway Company	9,809,395.58	
The Vermont Company	1,477,164.31	
Eastern Steamship Company		4,200,000.00
New York & Stamford Railway	1,395,523.40	
The Westchester Street Railroad	1,152,150.84	
Shore Line Electric Railroad		117,000.00
New England Investment and Security Company		13,631,750.00
	$74,599,953.46	$59,215,129.37

The true purpose of a statute is not punishment but the prevention of evil. When the force of a law has become so fully recognized that voluntary submission to it replaces recalcitrancy, its main purpose has been accomplished. Action in other parts of the country bears witness to conviction upon this point. The Missouri, Kansas & Texas in 1914, like the New Haven, came to an agreement under which a suit under the Anti-Trust law of Texas was withdrawn under promise of good behavior. This paved the way for the railroad to rehabilitate and even to consolidate its properties lawfully. The withdrawal from the anthracite coal combination of the Pennsylvania Railroad; its disposition of investments in competing trunk lines; the consolidation policy of the New York Central; the close scrutiny to which intercorporate relations are everywhere else being subjected; all alike demonstrate that the avowed purpose of the people to perpetuate railroad competition is accepted as an established fact.

XVI

EARLY SUPREME COURT DECISIONS: 1890–1901

THE KNIGHT CASE[1]

THE material facts proved are that the American Sugar Refining Company, one of the defendants, is incorporated under laws of New Jersey, and has authority to purchase, refine, and sell the sugar; that the Franklin Sugar Refinery, the E. C. Knight Company, the Spreckels Sugar Refinery, and the Delaware Sugar House, were incorporated under the laws of Pennsylvania, and authorized to purchase, refine, and sell sugar; that the four latter Pennsylvania companies were located in Philadelphia, and, prior to March, 1892, produced about thirty-three per cent of the total amount of sugar refined in the United States, and were in active competition with the American Sugar Refining Company, and with each other, selling their product wherever demand was found for it throughout the United States; that prior to March, 1892, the American Sugar Refining Company had obtained control of all refineries in the United States, excepting the four located in Philadelphia, and that of the Revere Company in Boston, the latter producing about two per cent of the amount refined in this country; that in March, 1892, the American Sugar Refining Company entered into contracts (on different dates) with the stockholders of each of the Philadelphia corporations named, whereby it purchased their stock, paying therefor by transfers of stock in its company; that the American Sugar Refining Company thus obtained possession of the Philadelphia refineries and their business; that each of the purchases was made subject to the American Sugar

[1] *U. S.* v. *E. C. Knight Co.*, 156 U. S. 1; Supreme Court Reporter, 249; decided March 26, 1894.

Refining Company obtaining authority to increase its stock \$25,000,000; that this assent was subsequently obtained, and the increase made; that there was no understanding or concert of action between the stockholders of the several Philadelphia companies respecting the sales, but that those of each company acted independently of those of the others, and in ignorance of what was being done by such others; that the stockholders of each company acted in concert with each other, understanding and intending that all the stock and property of the company should be sold; that the contract of sale in each instance left the sellers free to establish other refineries, and continue the business if they should see fit to do so, and contained no provision respecting trade or commerce in sugar, and that no arrangement or provision on this subject has been made since; that since the purchase the Delaware Sugar House Refinery has been operated in conjunction with the Spreckels Refinery, and the E. C. Knight Refinery in connection with the Franklin, this combination being made apparently for reasons of economy in conducting the business; that the amount of sugar refined in Philadelphia has been increased since the purchases; that the price has been slightly advanced since that event, but is still lower than it had been for some years before, and up to within a few months of the sales; that about ten per cent of the sugar refined and sold in the United States is refined in other refineries than those controlled by the American Sugar Refining Company; that some additional sugar is produced in Louisiana and some is brought from Europe, but the amount is not large in either instance.

The object in purchasing the Philadelphia refineries was to obtain a greater influence or more perfect control over the business of refining and selling sugar in this country.

The circuit court held that the facts did not show a contract, combination, or conspiracy to restrain or monopolize trade or commerce "among the several states or with foreign nations," and dismissed the bill. 60 Fed. 306. The cause was taken to the circuit court of appeals for the Third circuit, and the decree affirmed. 9 C. C. A. 297, 60 Fed. 934. This appeal was then prosecuted.

Mr. Chief Justice Fuller, after stating the facts in the foregoing language, delivered the opinion of the court.

By the purchase of the stock of the four Philadelphia refineries with shares of its own stock the American Sugar Refining Company acquired nearly complete control of the manufacture of refined sugar within the United States. The bill charged that the contracts under which these purchases were made constituted combinations in restraint of trade, and that in entering into them the defendants combined and conspired to restrain the trade and commerce in refined sugar among the several states and with foreign nations, contrary to the act of congress of July 2, 1890.

The relief sought was the cancellation of the agreements under which the stock was transferred, the redelivery of the stock to the parties respectively, and an injunction against the further performance of the agreements and further violations of the act. As usual, there was a prayer for general relief, but only such relief could be afforded under that prayer as would be agreeable to the case made by the bill and consistent with that specifically prayed. And as to the injunction asked, that relief was ancillary to and in aid of the primary equity, or ground of suit, and if that failed, would fall with it. That ground here was the existence of contracts to monopolize interstate or international trade or commerce, and to restrain such trade or commerce which, by the provisions of the act, could be rescinded, or operations thereunder arrested.

In commenting upon the statute (21 Jac. I. c. 3), at the commencement of chapter 85 of the third institute, entitled "Against Monopolists, Propounders, and Projectors," Lord Coke, in language often quoted, said:

It appeareth by the preamble of this act (as a judgment in parliament) that all grants of monopolies are against the ancient and fundamentall laws of this kingdome. And therefore it is necessary to define what a monopoly is.

A monopoly is an institution, or allowance by the king by his grant, commission, or otherwise to any person or persons, bodies politique, or corporate, of or for the sole buying, selling, making, working, or using of anything, whereby any person or persons, bodies politique, or

corporate, are sought to be restrained of any freedome or liberty that they had before, or hindred in their lawfull trade.

Counsel contend that this definition, as explained by the derivation of the word, may be applied to all cases in which "one person sells alone the whole of any kind of marketable thing, so that only he can continue to sell it, fixing the price at his own pleasure," whether by virtue of legislative grant or agreement; that the monopolization referred to in the act of congress is not confined to the common-law sense of the term as implying an exclusive control, by authority, of one branch of industry without legal right of any other person to interfere therewith by competition or otherwise, but that it includes engrossing as well, and covers controlling the market by contracts securing the advantage of selling alone or exclusively all, or some considerable portion, of a particular kind of merchandise or commodity to the detriment of the public; and that such contracts amount to that restraint of trade or commerce declared to be illegal. But the monopoly and restraint denounced by the act are the monopoly and restraint of interstate and international trade or commerce, while the conclusion to be assumed on this record is that the result of the transaction complained of was the creation of a monopoly in the manufacture of a necessary of life.

In the view which we take of the case, we need not discuss whether, because the tentacles which drew the outlying refineries into the dominant corporation were separately put out, therefore there was no combination to monopolize; or because, according to political economists, aggregations of capital may reduce prices, therefore the objection to concentration of power is relieved; or, because others were theoretically left free to go into the business of refining sugar, and the original stockholders of the Philadelphia refineries, after becoming stockholders of the American company, might go into competition with themselves, or, parting with that stock, might set up again for themselves, therefore no objectionable restraint was imposed.

The fundamental question is whether, conceding that the existence of a monopoly in manufacture is established by the

evidence, that monopoly can be directly suppressed under the act of congress in the mode attempted by this bill.

It cannot be denied that the power of a state to protect the lives, health, and property of its citizens, and to preserve good order and the public morals, "the power to govern men and things within the limits of its dominion," is a power originally and always belonging to the states, not surrendered by them to the general government, nor directly restrained by the constitution of the United States, and essentially exclusive. The relief of the citizens of each state from the burden of monopoly and the evils resulting from the restraint of trade among such citizens was left with the states to deal with, and this court has recognized their possession of that power even to the extent of holding that an employment or business carried on by private individuals, when it becomes a matter of such public interest and importance as to create a common charge or burden upon the citizen,—in other words, when it becomes a practical monopoly, to which the citizen is compelled to resort, and by means of which a tribute can be exacted from the community,—is subject to regulation by state legislative power. On the other hand, the power of congress to regulate commerce among the several states is also exclusive. The constitution does not provide that interstate commerce shall be free, but, by the grant of this exclusive power to regulate it, it was left free, except as congress might impose restraints. Therefore it has been determined that the failure of congress to exercise this exclusive power in any case is an expression of its will that the subject shall be free from restrictions or impositions upon it by the several states, and if a law passed by a state in the exercise of its acknowledged powers comes into conflict with that will, the congress and the state cannot occupy the position of equal opposing sovereignties, because the constitution declares its supremacy, and that of the laws passed in pursuance thereof; and that which is not supreme must yield to that which is supreme. "Commerce undoubtedly is traffic," said Chief Justice Marshall, "but it is something more; it is intercourse. It describes the commercial intercourse between nations and parts of nations in all its branches, and is regulated by prescribing rules for carry-

ing on that intercourse." That which belongs to commerce is within the jurisdiction of the United States, but that which does not belong to commerce is within the jurisdiction of the police power of the state.

The argument is that the power to control the manufacture of refined sugar is a monopoly over a necessary of life, to the enjoyment of which by a large part of the population of the United States interstate commerce is indispensable, and that, therefore, the general government, in the exercise of the power to regulate commerce, may repress such monopoly directly, and set aside the instruments which have created it. But this argument cannot be confined to necessaries of life merely, and must include all articles of general consumption. Doubtless the power to control the manufacture of a given thing involves, in a certain sense, the control of its disposition, but this is a secondary, and not the primary, sense; and, although the exercise of that power may result in bringing the operation of commerce into play, it does not control it, and affects it only incidentally and indirectly. Commerce succeeds to manufacture, and is not a part of it. The power to regulate commerce is the power to prescribe the rule by which commerce shall be governed, and is a power independent of the power to suppress monopoly. But it may operate in repression of monopoly whenever that comes within the rules by which commerce is governed, or whenever the transaction is itself a monopoly of commerce.

It is vital that the independence of the commercial power and of the police power, and the delimitation between them, however sometimes perplexing, should always be recognized and observed, for, while the one furnishes the strongest bond of union, the other is essential to the preservation of the autonomy of the states as required by our dual form of government; and acknowledged evils, however grave and urgent they may appear to be, had better be borne, than the risk be run, in the effort to suppress them, of more serious consequences by resort to expedients of even doubtful constitutionality.

It will be perceived how far-reaching the proposition is that the power of dealing with a monopoly directly may be exercised by the general government whenever interstate or international

commerce may be ultimately affected. The regulation of commerce applies to the subjects of commerce, and not to matters of internal police. Contracts to buy, sell, or exchange goods to be transported among the several states, the transportation and its instrumentalities, and articles bought, sold, or exchanged for the purposes of such transit among the states, or put in the way of transit, may be regulated; but this is because they form part of interstate trade or commerce. The fact that an article is manufactured for export to another state does not of itself make it an article of interstate commerce, and the intent of the manufacturer does not determine the time when the article or product passes from the control of the state and belongs to commerce. This was so ruled in *Coe* v. *Errol*, 116 U. S. 517, 6 Sup. Ct. 475, in which the question before the court was whether certain logs cut at a place in New Hampshire, and hauled to a river town for the purpose of transportation to the state of Maine, were liable to be taxed like other property in the state of New Hampshire. Mr. Justice Bradley, delivering the opinion of the court, said:

Does the owner's state of mind in relation to the goods—that is, his intent to export them, and his partial preparation to do so—exempt them from taxation? This is the precise question for solution. . . . There must be a point of time when they cease to be governed exclusively by the domestic law, and begin to be governed and protected by the national law of commercial regulation; and that moment seems to us to be a legitimate one for this purpose in which they commence their final movement from the state of their origin to that of their destination.

And again, in *Kidd* v. *Pearson*, 128 U. S. 1, 20, 24, 9 Sup. Ct. 6, where the question was discussed whether the right of a state to enact a statute prohibiting within its limits the manufacture of intoxicating liquors, except for certain purposes, could be overthrown by the fact that the manufacturer intended to export the liquors when made, it was held that the intent of the manufacturer did not determine the time when the article or product passed from the control of the state and belonged to commerce, and that, therefore, the statute, in omitting to except

from its operation the manufacture of intoxicating liquors within the limits of the state for export, did not constitute an unauthorized interference with the right of congress to regulate commerce. And Mr. Justice Lamar remarked:

No distinction is more popular to the common mind, or more clearly expressed in economic and political literature, than that between manufacture and commerce. Manufacture is transformation,—the fashioning of raw materials into a change of form for use. The functions of commerce are different. The buying and selling, and the transportation incidental thereto, constitute commerce: and the regulation of commerce in the constitutional sense embraces the regulation at least of such transportation. . . . If it be held that the term includes the regulation of all such manufacturers as are intended to be the subject of commercial transactions in the future, it is impossible to deny that it would also include all productive industries that contemplate the same thing. The result would be that congress would be invested, to the exclusion of the states, with the power to regulate, not only manufactures, but also agriculture, horticulture, stock-raising, domestic fisheries, mining; in short, every branch of human industry. For is there one of them that does not contemplate, more or less clearly, an interstate or foreign market? Does not the wheat grower of the Northwest, and the cotton planter of the South, plant, cultivate, and harvest his crop with an eye on the prices at Liverpool, New York, and Chicago? The power being vested in congress and denied to the states, it would follow as an inevitable result that the duty would devolve on congress to regulate all of these delicate multiform, and vital interests,—interests which in their nature are, and must be, local in all the details of their successful management. . . . The demands of such supervision would require, not uniform legislation generally applicable throughout the United States, but a swarm of statutes only locally applicable, and utterly inconsistent. Any movement towards the establishment of rules of production in this vast country, with its many different climates and opportunities, would only be at the sacrifice of the peculiar advantages of a large part of the localities in it, if not of every one of them. On the other hand, any movement towards the local, detailed, and incongruous legislation required by such interpretation would be about the widest possible departure from the declared object of the clause in question. Nor this alone. Even in the exercise of the power contended for, congress would be confined to the regulation, not of certain branches of in-

dustry, however numerous, but to those instances in each and every branch where the producer contemplated an interstate market. These instances would be almost infinite, as we have seen; but still there would always remain the possibility, and often it would be the case, that the producer contemplated a domestic market. In that case the supervisory power must be executed by the state; and the interminable trouble would be presented that whether the one power or the other should exercise the authority in question would be determined, not by any general or intelligible rule, but by the secret and changeable intention of the producer in each and every act of production. A situation more paralyzing to the state governments, and more provocative of conflicts between the general government and the states, and less likely to have been what the framers of the constitution intended, it would be difficult to imagine.

And see *Veazie* v. *Moor*, 14 How. 568, 574.

In *Gibbons* v. *Ogden*, *Brown* v. *Maryland*, and other cases often cited, the state laws, which were held inoperative, were instances of direct interference with, or regulations of, interstate or international commerce; yet in *Kidd* v. *Pearson* the refusal of a state to allow articles to be manufactured within her borders, even for export, was held not to directly affect external commerce; and state legislation which, in a great variety of ways, affected interstate commerce and persons engaged in it, has been frequently sustained because the interference was not direct.

Contracts, combinations, or conspiracies to control domestic enterprise in manufacture, agriculture, mining, production in all its forms, or to raise or lower prices or wages, might unquestionably tend to restrain external as well as domestic trade, but the restraint would be an indirect result, however inevitable, and whatever its extent, and such result would not necessarily determine the object of the contract, combination, or conspiracy.

Again, all the authorities agree that, in order to vitiate a contract or combination, it is not essential that its result should be a complete monopoly; it is sufficient if it really tends to that end, and to deprive the public of the advantages which flow from free competition. Slight reflection will show that, if the national power extends to all contracts and combinations in manufacture, agriculture, mining, and other productive indus-

tries, whose ultimate result may affect external commerce, comparatively little of business operations and affairs would be left for state control.

It was in the light of well-settled principles that the act of July 2, 1890, was framed. Congress did not attempt thereby to assert the power to deal with monopoly directly as such; or to limit and restrict the rights of corporations created by the states or the citizens of the states in the acquisition, control, or disposition of property; or to regulate or prescribe the price or prices at which such property or the products thereof should be sold; or to make criminal the acts of persons in the acquisition and control of property which the states of their residence or creation sanctioned or permitted. Aside from the provisions applicable where congress might exercise municipal power, what the law struck at was combinations, contracts, and conspiracies to monopolize trade and commerce among the several states or with foreign nations; but the contracts and acts of the defendants related exclusively to the acquisition of the Philadelphia refineries and the business of sugar refining in Pennsylvania, and bore no direct relation to commerce between the states or with foreign nations. The object was manifestly private gain in the manufacture of the commodity, but not through the control of interstate or foreign commerce. It is true that the bill alleged that the products of these refineries were sold and distributed among the several states, and that all the companies were engaged in trade or commerce with the several states and with foreign nations; but this was no more than to say that trade and commerce served manufacture to fulfill its function. Sugar was refined for sale, and sales were probably made at Philadelphia for consumption, and undoubtedly for resale by the first purchasers throughout Pennsylvania and other states, and refined sugar was also forwarded by the companies to other states for sale. Nevertheless it does not follow that an attempt to monopolize, or the actual monopoly of, the manufacture was an attempt, whether executory or consummated, to monopolize commerce, even though, in order to dispose of the product, the instrumentality of commerce was necessarily invoked. There was nothing in the proofs to indicate any intention to put a restraint

upon trade or commerce, and the fact, as we have seen, that trade or commerce might be indirectly affected, was not enough to entitle complainants to a decree. The subject-matter of the sale was shares of manufacturing stock, and the relief sought was the surrender of property which had already passed, and the suppression of the alleged monopoly in manufacture by the restoration of the *status quo* before the transfers; yet the act of congress only authorized the circuit courts to proceed by way of preventing and restraining violations of the act in respect of contracts, combinations, or conspiracies in restraint of interstate or international trade or commerce.

The Circuit Court declined, upon the pleadings and proofs, to grant the relief prayed, and dismissed the bill, and we are of opinion that the Circuit Court of Appeals did not err in affirming that decree.

Decree affirmed.

Mr. Justice Harlan, dissenting.

What is commerce among the states? The decisions of this court fully answer the question. "Commerce, undoubtedly, is traffic, but it is something more; it is intercourse." It does not embrace the completely interior traffic of the respective states,— that which is "carried on between man and man in a state, or between different parts of the same state, and which does not extend to or affect other states,"—but it does embrace "every species of commercial intercourse" between the United States and foreign nations and among the states, and therefore it includes such traffic or trade, buying, selling, and interchange of commodities, as directly affects or necessarily involves the interests of the people of the United States. "Commerce, as the word is used in the constitution, is a unit," and "cannot stop at the external boundary line of each state, but may be introduced into the interior." "The genius and character of the whole government seem to be that its action is to be applied to all the external concerns of the nation, and to those internal concerns which affect the states generally."

These principles were announced in *Gibbons* v. *Ogden*, and have often been approved. It is the settled doctrine of this court that interstate commerce embraces something more than the

mere physical transportation of articles of property, and the vehicles or vessels by which such transportation is effected. Interstate commerce does not, therefore, consist in transportation simply. It includes the purchase and sale of articles that are intended to be transported from one state to another, — every species of commercial intercourse among the states and with foreign nations.

The fundamental inquiry in this case is, what in a legal sense is an unlawful restraint of trade?

Sir William Erle, formerly chief justice of the common pleas, in his essay on the Law Relating to Trade Unions, well said that "restraint of trade, according to a general principle of the common law, is unlawful"; that "at common law every person has individually, and the public also have collectively, a right to require that the course of trade should be kept free from unreasonable obstruction"; and that "the right to a free course for trade is of great importance to commerce and productive industry, and has been carefully maintained by those who have administered the common law."

There is a partial restraint of trade which, in certain circumstances, is tolerated by the law. The rule upon that subject is stated in *Navigation Co.* v. *Winsor*, 20 Wall. 64, 66, where it was said that:

> An agreement in general restraint of trade is illegal and void; but an agreement which operates merely in partial restraint of trade is good, provided it be not unreasonable, and there be a consideration to support it. In order that it may not be unreasonable, the restraint imposed must not be larger than is required for the necessary protection of the party with whom the contract is made. A contract, even on good consideration, not to use a trade anywhere in England is held void in that country as being too general a restraint of trade.
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> *Horner* v. *Graves*, 7 Bing. 743.

But a general restraint of trade has often resulted from combinations formed for the purpose of controlling prices by destroying the opportunity of buyers and sellers to deal with each other upon the basis of fair, open, free competition. Combinations of this character have frequently been the subject of judicial

scrutiny, and have always been condemned as illegal because of their necessary tendency to restrain trade. Such combinations are against common right, and are crimes against the public. To some of the cases of that character it will be well to refer.

In *Morris Run Coal Co.* v. *Barclay Coal Co.*, 68 Pa. St. 173, 183-187, the principal question was as to the validity of a contract made between five coal corporations of Pennsylvania, by which they divided between themselves two coal regions of which they had the control. The referee in the case found that those companies acquired under their arrangement the power to control the entire market for bituminous coal in the northern part of the state, and their combination was, therefore, a restraint upon trade, and against public policy. In response to the suggestion that the real purpose of the combination was to lessen expenses, to advance the quality of coal, and to deliver it in the markets intended to be supplied in the best order to the consumer, the supreme court of Pennsylvania said:

This is denied by the defendants, but it seems to us it is immaterial whether these positions are sustained or not. Admitting their correctness, it does not follow that these advantages redeem the contract from the obnoxious effects so strikingly presented by the referee. The important fact is that these companies control this immense coal field; that it is the great source of supply of bituminous coal to the state of New York and large territories westward; that by this contract they control the price of coal in this extensive market, and make it bring sums it would not command if left to the natural laws of trade; that it concerns an article of prime necessity for many uses; that its operation is general in this large region, and affects all who use coal as a fuel, and this is accomplished by a combination of all the companies engaged in this branch of business in the large region where they operate. The combination is wide in scope, general in its influence, and injurious in effects. These being its features, the contract is against public policy, illegal, and therefore void.

Again, in the same case:

The effects produced on the public interests lead to the consideration of another feature of great weight in determining the illegality of the contract, to wit, the combination resorted to by these five companies. Singly each might have suspended deliveries and sales of

coal to suit its own interests, and might have raised the price, even though this might have been detrimental to the public interest. There is a certain freedom which must be allowed to everyone in the management of his own affairs. When competition is left free, individual error or folly will generally find a corrective in the conduct of others. But here is a combination of all the companies operating in the Blossburg and Barclay regions, and controlling their entire productions. They have combined together to govern the supply and the price of coal in all the markets from the Hudson to the Mississippi rivers, and from Pennsylvania to the Lakes. This combination has a power in its confederated form which no individual action can confer. The public interest must succumb to it, for it has left no competition free to correct its baleful influence. When the supply of coal is suspended, the demand for it becomes importunate, and prices must rise; or, if the supply goes forward, the price fixed by the confederates must accompany it. The domestic hearth, the furnaces of the iron master, and the fires of the manufacturer all feel the restraint, while many dependent hands are paralyzed, and hungry mouths are stinted. The influence of a lack of supply or a rise in the price of an article of such prime necessity cannot be measured. It permeates the entire mass of the community, and leaves few of its members untouched by its withering blight. Such a combination is more than a contract; it is an offense. "I take it," said Gibson, J., "a combination is criminal whenever the act to be done has a necessary tendency to prejudice the public or to oppress individuals, by unjustly subjecting them to the power of the confederates, and giving effect to the purpose of the latter, whether of extortion or of mischief." *Com.* v. *Carlisle*, Brightly, N. P. 40. In all such combinations where the purpose is injurious or unlawful, the gist of the offence is the conspiracy. Men can often do by the combination of many what severally no one could accomplish, and even what, when done by one, would be innocent. There is a potency in numbers when combined which the law cannot overlook, where injury is the consequence.

These principles were applied in *People* v. *Chicago Gas Trust Co.*, 130 Ill. 269, 292, 297, 22 N. E. 798, which involved the validity of a corporation formed for the purpose of operating gas works, and of manufacturing and selling gas, and which, for the purpose of destroying competition, acquired the stock of four other gas companies, and thereby obtained a monopoly in the business of furnishing illuminating gas to the city of Chicago

and its inhabitants. The court, in declaring the organization of the company to be illegal, said:

The fact that the appellee, almost immediately after its organization, bought up a majority of the shares of stock of each of these companies, shows that it was not making a mere investment of surplus funds, but that it designed and intended to bring the four companies under its control, and by crushing out competition, to monopolize the gas business in Chicago. Of what avail, [said the court,] is it that any number of gas companies may be formed under the general incorporation law, if a giant trust company can be clothed with the power of buying up and holding the stock and property of such companies, and, through the control thereby attained, can direct all their operations, and weld them into one huge combination?

A leading case on the question as to what combinations are illegal as being in general restraint of trade is *Richardson* v. *Buhl*, 77 Mich. 632, 635, 657, 660, 43 N. W. 1102, which related to certain agreements connected with the business and operations of the Diamond Match Company. From the report of the case it appears that that company was organized, under the laws of Connecticut, for the purpose of uniting in one corporation all the match manufactories in the United States, and to monopolize and control the business of making all the friction matches in the country, and establish the price thereof. To that end it became necessary, among other things, to buy many plants that had become established or were about to be established, as well as the property used in connection therewith. Chief Justice Sherwood of the supreme court of Michigan said:

The sole object of the corporation is to make money by having it in its power to raise the price of the article, or diminish the quantity to be made and used, at its pleasure. Thus both the supply of the article and the price thereof are made to depend upon the action of a half dozen individuals, more or less, to satisfy their cupidity and avarice, who may happen to have the controlling interest in this corporation, — an artificial person, governed by a single motive or purpose, which is to accumulate money regardless of the wants or necessities of over 60,000,000 people. The article thus completely under their control for the last fifty years has come to be regarded as one of necessity, not only in every household in the land, but one of daily use

by almost every individual in the country. It is difficult to conceive of a monopoly which can affect a greater number of people, or one more extensive in its effect on the country, than that of the Diamond Match Company. It was to aid that company in its purposes and in carrying out its object that the contract in this case was made between those parties, and which we are now asked to aid in enforcing. Monopoly in trade, or in any kind of business in this country, is odious to our form of government. It is sometimes permitted to aid the government in carrying on a great public enterprise or public work under governmental control in the interest of the public. Its tendency is, however, destructive of free institutions, and repugnant to the instincts of a free people, and contrary to the whole scope and spirit of the federal constitution, and is not allowed to exist under express provisions in several of our state constitutions. . . . All combinations among persons or corporations for the purpose of raising or controlling the prices of merchandise, or any of the necessaries of life, are monopolies, and intolerable; and ought to receive the condemnation of all courts.

This extended reference to adjudged cases relating to unlawful restraints upon the interior traffic of a state has been made for the purpose of showing that a combination such as that organized under the name of the American Sugar Refining Company has been uniformly held by the courts of the states to be against public policy, and illegal, because of its necessary tendency to impose improper restraints upon trade. And such, I take it, would be the judgment of any circuit court of the United States in a case between parties in which it became necessary to determine the question. The judgments of the state courts rest upon general principles of law, and not necessarily upon statutory provisions expressly condemning restraints of trade imposed by or resulting from combinations. Of course, in view of the authorites, it will not be doubted that it would be competent for a state, under the power to regulate its domestic commerce, and for the purpose of protecting its people against fraud and injustice, to make it a public offense, punishable by fine and imprisonment, for individuals or corporations to make contracts, form combinations, or engage in conspiracies, which unduly restrain trade or commerce carried on within its limits, and also to authorize the institution of proceedings for the pur-

pose of annulling contracts of that character, as well as of preventing or restraining such combinations and conspiracies.

But there is a trade among the several states which is distinct from that carried on within the territorial limits of a state. The regulation and control of the former are committed by the national constitution to congress. Commerce among the states, as this court has declared, is a unit, and in respect of that commerce this is one country, and we are one people. It may be regulated by rules applicable to every part of the United States, and state lines and state jurisdiction cannot interfere with the enforcement of such rules. The jurisdiction of the general government extends over every foot of territory within the United States. Under the power with which it is invested, congress may remove unlawful obstructions, of whatever kind, to the free course of trade among the states. In so doing it would not interfere with the "autonomy of the states," because the power thus to protect interstate commerce is expressly given by the people of all the states. Interstate intercourse, trade, and traffic are absolutely free, except as such intercourse, trade, or traffic may be incidentally or indirectly affected by the exercise by the states of their reserved police powers. *Sherlock* v. *Alling*, 99 U. S. 99, 103. It is the constitution, the supreme law of the land, which invests congress with power to protect commerce among the states against burdens and exactions arising from unlawful restraints by whatever authority imposed. Surely, a right secured or granted by that instrument is under the protection of the government which that instrument creates. Any combination, therefore, that disturbs or unreasonably obstructs freedom in buying and selling articles manufactured to be sold to persons in other states, or to be carried to other states,—a freedom that cannot exist if the right to buy and sell is fettered by unlawful restraints that crush out competition,—affects, not incidentally, but directly, the people of all the states; and the remedy for such an evil is found only in the exercise of powers confided to a government which, this court has said, was the government of all, exercising powers delegated by all, representing all, acting for all. *M'Culloch* v. *Maryland*, 4 Wheat. 405.

It may be admitted that an act which did nothing more than

forbid, and which had no other object than to forbid, the mere refining of sugar in any state, would be in excess of any power granted to congress. But the act of 1890 is not of that character. It does not strike at the manufacture simply of articles that are legitimate or recognized subjects of commerce, but at combinations that unduly restrain, because they monopolize, the buying and selling of articles which are to go into interstate commerce. In *State* v. *Stewart*, 59 Vt. 273, 286, 9 Atl. 559, it was said that if a combination of persons "seek to restrain trade, or tend to the destruction of the material property of the country, they work injury to the whole people." And in *State* v. *Glidden*, 55 Conn. 46, 75, 8 Atl. 890, the court said:

> Any one man, or any one of several men acting independently, is powerless; but when several combine, and direct their united energies to the accomplishment of a bad purpose, the combination is formidable. Its power for evil increases as its number increases. . . . The combination becomes dangerous and subversive of the rights of others, and the law wisely says it is a crime.

Chief Justice Gibson well said in *Com.* v. *Carlisle*, Brightly N. P. 36, 39, 40:

> There is between the different parts of the body politic a reciprocity of action on each other, which, like the action of antagonizing muscles in the natural body, not only prescribes to each its appropriate state and action, but regulates the motion of the whole. The effort of an individual to disturb this equilibrium can never be perceptible, nor carry the operation of his interest, or that of any other individual, beyond the limits of fair competition; but the increase of power by combination of means being in geometrical proportion to the number concerned, an association may be able to give an impulse, not only oppressive to individuals, but mischievous to the public at large; and it is the employment of an engine so powerful and dangerous that gives criminality to an act that would be perfectly innocent, at least in a legal view, when done by an individual.

These principles underlie the act of congress, which has for its sole object the protection of such trade and commerce as the constitution confides to national control, and the question is presented whether the combination assailed by this suit is an

unlawful restraint upon interstate trade in a necessary article of food, which, as every one knows, has always entered, now enters, and must continue to enter, in vast quantities, into commerce among the states.

In *Kidd* v. *Pearson* we recognized, as had been done in previous cases, the distinction between the mere transportation of articles of interstate commerce and the purchasing and selling that precede transportation It is said that manufacture precedes commerce, and is not a part of it. But it is equally true that when manufacture ends, that which has been manufactured becomes a subject of commerce; that buying and selling succeed manufacture, come into existence after the process of manufacture is completed, precede transportation, and are as much commercial intercourse, where articles are bought to be carried from one state to another, as is the manual transportation of such articles after they have been so purchased. The distinction was recognized by this court in *Gibbons* v. *Ogden*, where the principal question was whether commerce included navigation. Both the court and counsel recognized buying and selling or barter as included in commerce. Chief Justice Marshall said that the mind can scarcely conceive a system for regulating commerce, which was "confined to prescribing rules for the conduct of individuals in the actual employment of buying and selling, or of barter." Pages 189, 190, 9 Wheat.

The power of congress covers and protects the absolute freedom of such intercourse and trade among the states as may or must succeed manufacture and precede transportation from the place of purchase. This would seem to be conceded, for the court in the present case expressly declare that "contracts to buy, sell, or exchange goods to be transported among the several states, the transportation and its instrumentalities, and articles bought, sold, or exchanged for the purpose of such transit among the states, or put in the way of transit, may be regulated, but this is because they form part of interstate trade or commerce." Here is a direct admission — one which the settled doctrines of this court justify — that contracts to buy, and the purchasing of goods to be transported from one state to another, and transportation, with its instrumentalities, are all parts of

interstate trade or commerce. Each part of such trade is then under the protection of congress. And yet, by the opinion and judgment in this case, if I do not misapprehend them, congress is without power to protect the commercial intercourse that such purchasing necessarily involves against the restraints and burdens arising from the existence of combinations that meet purchasers, from whatever state they come, with the threat — for it is nothing more nor less than a threat — that they shall not purchase what they desire to purchase, except at the prices fixed by such combinations. A citizen of Missouri has the right to go in person, or send orders, to Pennsylvania and New Jersey for the purpose of purchasing refined sugar. But of what value is that right if he is confronted in those states by a vast combination, which absolutely controls the price of that article by reason of its having acquired all the sugar refineries in the United States in order that they may fix prices in their own interest exclusively?

In my judgment, the citizens of the several states composing the Union are entitled of right to buy goods in the state where they are manufactured, or in any other state, without being confronted by an illegal combination whose business extends throughout the whole country, which, by the law everywhere, is an enemy to the public interests, and which prevents such buying, except at prices arbitrarily fixed by it. I insist that the free course of trade among the states cannot coexist with such combinations. When I speak of trade I mean the buying and selling of articles of every kind that are recognized articles of interstate commerce. Whatever improperly obstructs the free course of interstate intercourse and trade, as involved in the buying and selling of articles to be carried from one state to another, may be reached by congress under its authority to regulate commerce among the states. The exercise of that authority so as to make trade among the states in all recognized articles of commerce absolutely free from unreasonable or illegal restrictions imposed by combinations is justified by an express grant of power to congress, and would redound to the welfare of the whole country. I am unable to perceive that any such result would imperil the autonomy of the states, especially as

that result cannot be attained through the action of any one state.

Undue restrictions or burdens upon the purchasing of goods in the market for sale, to be transported to other states, cannot be imposed, even by a state, without violating the freedom of commercial intercourse guaranteed by the constitution. But if a state within whose limits the business of refining sugar is exclusively carried on may not constitutionally impose burdens upon purchases of sugar to be transported to other states, how comes it that combinations of corporations or individuals within the same state may not be prevented by the national government from putting unlawful restraints upon the purchasing of that article to be carried from the state in which such purchases are made? If the national power is competent to repress state action in restraint of interstate trade as it may be involved in purchases of refined sugar to be transported from one state to another state, surely it ought to be deemed sufficient to prevent unlawful restraints attempted to be imposed by combinations of corporations or individuals upon those identical purchases; otherwise illegal combinations of corporations or individuals may — so far as national power and interstate commerce are concerned — do with impunity what no state can do.

Suppose that a suit were brought in one of the courts of the United States — jurisdiction being based, it may be, alone upon the diverse citizenship of the parties — to enforce the stipulations of a written agreement, which had for its object to acquire the possession of all the sugar refineries in the United States, in order that those engaged in the combination might obtain the entire control of the business of refining and selling sugar throughout the country, and thereby to increase or diminish prices as the particular interests of the combination might require. I take it that the court, upon recognized principles of law common to the jurisprudence of this country and of Great Britain, would deny the relief asked, and dismiss the suit upon the ground that the necessary tendency of such an agreement and combination was to restrain not simply trade that was completely internal to the state in which the parties resided, but trade and commerce among all the states, and was, there-

fore, against public policy, and illegal. If I am right in this view, it would seem to follow, necessarily, that congress could enact a statute forbidding such combinations so far as they affected interstate commerce, and provide for their suppression as well through civil proceedings instituted for that purpose as by penalties against those engaged in them.

In committing to congress the control of commerce with foreign nations and among the several states, the constitution did not define the means that may be employed to protect the freedom of commercial intercourse and traffic established for the benefit of all the people of the Union. It wisely forbore to impose any limitations upon the exercise of that power except those arising from the general nature of the government, or such as are embodied in the fundamental guaranties of liberty and property. It gives to congress, in express words, authority to enact all laws necessary and proper for carrying into execution the power to regulate commerce; and whether an act of congress, passed to accomplish an object to which the general government is competent, is within the power granted, must be determined by the rule announced through Chief Justice Marshall three quarters of a century ago, and which has been repeatedly affirmed by this court. That rule is:

> The sound construction of the constitution must allow to the national legislature the discretion with respect to the means by which the powers it confers are to be carried into execution, which will enable that body to perform the high duties assigned to it in the manner most beneficial to the people. Let the end be legitimate, let it be within the scope of the constitution; and all means which are appropriate, which are plainly adapted to that end, which are not prohibited, but consistent with the letter and spirit of the constitution, are constitutional.
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> *M'Culloch* v. *Maryland*, 4 Wheat. 316, 421.

The end proposed to be accomplished by the act of 1890 is the protection of trade and commerce among the states against unlawful restraints. Who can say that that end is not legitimate, or is not within the scope of the constitution? The means employed are the suppression, by legal proceedings, of combinations, con-

spiracies, and monopolies which, by their inevitable and admitted tendency, improperly restrain trade and commerce among the states. Who can say that such means are not appropriate to attain the end of freeing commercial intercourse among the states from burdens and exactions imposed upon it by combinations which, under principles long recognized in this country, as well as at the common law, are illegal and dangerous to the public welfare? What clause of the constitution can be referred to which prohibits the means thus prescribed in the act of congress?

It may be that the means employed by congress to suppress combinations that restrain interstate trade and commerce are not all or the best that could have been devised. But congress, under the delegation of authority to enact laws necessary and proper to carry into effect a power granted, is not restricted to the employment of those means "without which the end would be entirely unattainable."

To have prescribed the means, [this court has said,] by which government should, in all future time, execute its powers, would have been to change entirely the character of that instrument, and give it the properties of a legal code. It would have been an unwise attempt to provide by immutable rules for exigencies which, if foreseen at all, must have been seen dimly, and which can be best provided for as they occur. To have declared that the best means shall not be used, but those alone without which the power given would be nugatory, would have been to deprive the legislature of the capacity to avail itself of experience, to exercise its reason, and to accommodate its legislation to circumstances.

Again:

Where the law is not prohibited, and is really calculated to effect any of the objects intrusted to the government, to undertake here to inquire into the degree of its necessity would be to pass the line which circumscribes the judicial department, and to tread on legislative ground.

M'Culloch v. *Maryland*, 4 Wheat. 316, 415, 423.

By the act of 1890, congress subjected to forfeiture "any property owned under any contract or by any combination, or pursuant to any conspiracy (and being the subject thereof)

mentioned in section one of this act, and being in the course of transportation from one state to another, or to a foreign country." It was not deemed wise to subject such property to forfeiture before transportation began or after it ended. If it be suggested that congress might have prohibited the transportation from the state in which they are manufactured any articles, by whomsoever at the time owned, that had been manufactured by combinations formed to monopolize some designated part of trade or commerce among the states, my answer is that it is not within the functions of the judiciary to adjudge that congress shall employ particular means in execution of a given power, simply because such means are, in the judgment of the courts, best conducive to the end sought to be accomplished. Congress, in the exercise of its discretion as to choice of means conducive to an end to which it was competent, determined to reach that end through civil proceedings, instituted to prevent or restrain these obnoxious combinations in their attempts to burden interstate commerce by obstructions that interfere in advance of transportation with the course of trade between the people of the states. In other words congress sought to prevent the coming into existence of combinations the purpose or tendency of which was to impose unlawful restraints upon interstate commerce.

The question here relates to restraints upon the freedom of interstate trade and commerce imposed by illegal combinations. After the fullest consideration I have been able to bestow upon this important question, I find it impossible to refuse my assent to this proposition: Whatever a state may do to protect its completely interior traffic or trade against unlawful restraints, the general government is empowered to do for the protection of the people of all the states — for this purpose, one people — against unlawful restraints imposed upon interstate traffic or trade in articles that are to enter into commerce among the several states. If, as already shown, a state may prevent or suppress a combination, the effect of which is to subject its domestic trade to the restraints necessarily arising from their obtaining the absolute control of the sale of a particular article in general use by the community, there ought to be no hesitation in allowing to congress the right to suppress a similar com-

bination that imposes a like unlawful restraint upon interstate trade and traffic in that article. While the states retain, because they have never surrendered, full control of their completely internal traffic, it was not intended by the framers of the constitution that any part of interstate commerce should be excluded from the control of congress. Each state can reach and suppress combinations so far as they unlawfully restrain its interior trade, while the national government may reach and suppress them so far as they unlawfully restrain trade among the states.

While the opinion of the court in this case does not declare the act of 1890 to be unconstitutional, it defeats the main object for which it was passed, for it is, in effect, held that the statute would be unconstitutional if interpreted as embracing such unlawful restraints upon the purchasing of goods in one state to be carried to another state as necessarily arise from the existence of combinations formed for the purpose and with the effect, not only of monopolizing the ownership of all such goods in every part of the country, but of controlling the prices for them in all the states. This view of the scope of the act leaves the public, so far as national power is concerned, entirely at the mercy of combinations which arbitrarily control the prices of articles purchased to be transported from one state to another state. I cannot assent to that view. In my judgment, the general government is not placed by the constitution in such a condition of helplessness that it must fold its arms and remain inactive while capital combines, under the name of a corporation, to destroy competition, not in one state only, but throughout the entire country, in the buying and selling of articles — especially the necessaries of life — that go into commerce among the states. The doctrine of the autonomy of the states cannot properly be invoked to justify a denial of power in the national government to meet such an emergency, involving, as it does, that freedom of commercial intercourse among the states which the constitution sought to attain.

It is said that there are no proofs in the record which indicate an intention upon the part of the American Sugar Refining Company and its associates to put a restraint upon trade or

commerce. Was it necessary that formal proof be made that the persons engaged in this combination admitted in words that they intended to restrain trade or commerce? Did any one expect to find in the written agreements which resulted in the formation of this combination a distinct expression of a purpose to restrain interstate trade or commerce? Men who form and control these combinations are too cautious and wary to make such admissions orally or in writing. Why, it is conceded that the object of this combination was to obtain control of the business of making and selling refined sugar throughout the entire country. Those interested in its operations will be satisfied with nothing less than to have the whole population of America pay tribute to them. That object is disclosed upon the very face of the transactions described in the bill. And it is proved — indeed, is conceded — that that object has been accomplished to the extent that the American Sugar Refining Company now controls 98 per cent of all the sugar refining business in the country, and therefore controls the price of that article everywhere. Now, the mere existence of a combination having such an object and possessing such extraordinary power is itself, under settled principles of law, — there being no adjudged case to the contrary in this country, — a direct restraint of trade in the article for the control of the sales of which in this country that combination was organized. And that restraint is felt in all the states, for the reason, known to all, that the article in question goes, was intended to go, and must always go, into commerce among the several states, and into the homes of people in every condition of life.

A decree recognizing the freedom of commercial intercourse as embracing the right to buy goods to be transported from one state to another without buyers being burdened by unlawful restraints imposed by combinations of corporations or individuals, so far from disturbing or endangering would tend to preserve the autonomy of the states, and protect the people of all states against dangers so portentous as to excite apprehension for the safety of our liberties. If this be not a sound interpretation of the constitution, it is easy to perceive that interstate traffic, so far as it involves the price to be paid for articles nec-

essary to the comfort and well-being of the people in all the states, may pass under the absolute control of overshadowing combinations having financial resources without limit, and an audacity in the accomplishment of their objects that recognizes none of the restraints of moral obligations controlling the action of individuals; combinations governed entirely by the law of greed and selfishness, so powerful that no single state is able to overthrow them, and give the required protection to the whole country, and so all-pervading that they threaten the integrity of our institutions.

We have before us the case of a combination which absolutely controls, or may, at its discretion, control, the price of all refined sugar in this country. Suppose another combination, organized for private gain and to control prices, should obtain possession of all the large flour mills in the United States; another, of all the grain elevators; another, of all the oil territory; another, of all the salt-producing regions; another, of all the cotton mills; and another, of all the great establishments for slaughtering animals and the preparation of meats. What power is competent to protect the people of the United States against such dangers except a national power, — one that is capable of exerting its sovereign authority throughout every part of the territory and over all the people of the nation?

To the general government has been committed the control of commercial intercourse among the states, to the end that it may be free at all times from any restraints except such as congress may impose or permit for the benefit of the whole country. The common government of all the people is the only one that can adequately deal with a matter which directly and injuriously affects the entire commerce of the country, which concerns equally all the people of the Union, and which, it must be confessed, cannot be adequately controlled by any one state. Its authority should not be so weakened by construction that it cannot reach and eradicate evils that, beyond all question, tend to defeat an object which that government is entitled, by the constitution, to accomplish.

Powerful and ingenious minds, [this court has said,] taking, as postulates, that the powers expressly granted to the government of the

Union are to be contracted by construction into the narrowest possible compass, and that the original powers of the states are retained, if any possible construction will retain them, may, by a course of well-digested but refined and metaphysical reasoning, founded on these premises, explain away the constitution of our country, and leave it a magnificent structure, indeed, to look at, but totally unfit for use. They may so entangle and perplex the understanding as to obscure principles which were before thought quite plain, and induce doubts where, if the mind were to pursue its own course, none would be perceived.

Gibbons v. *Ogden*, 9 Wheat. 1, 222.

While a decree annulling the contracts under which the combination in question was formed may not, in view of the facts disclosed, be effectual to accomplish the object of the act of 1890, I perceive no difficulty in the way of the court passing a decree declaring that that combination imposes an unlawful restraint upon trade and commerce among the states, and perpetually enjoining it from further prosecuting any business pursuant to the unlawful agreements under which it was formed, or by which it was created. Such a decree would be within the scope of the bill, and is appropriate to the end which congress intended to accomplish, namely, to protect the freedom of commercial intercourse among the states against combinations and conspiracies which impose unlawful restraints upon such intercourse.

For the reasons stated, I dissent from the opinion and judgment of the court.

THE ADDYSTONE PIPE CASE[1]

Assuming, for the purpose of the argument, that the contract in question herein does directly and substantially operate as a restraint upon and as a regulation of interstate commerce, it is yet insisted by the appellants at the threshold of the inquiry that by the true construction of the Constitution, the power of Congress to regulate interstate commerce is limited to its protection

[1] *Addystone Pipe & Steel Co.* v. *U. S.*, 175 U. S. 211; 20 Supreme Court Reporter, 97; rendered December 4, 1899. The material facts are set forth in Chapter IV, *supra*, and are therefore omitted herein. This states merely the law.

from acts of interference by state legislation or by means of regulations made under the authority of the state by some political subdivision thereof, including also congressional power over common carriers, elevator, gas, and water companies, for reasons stated to be peculiar to such carriers and companies, but that it does not include the general power to interfere with or prohibit private contracts between citizens, even though such contracts have interstate commerce for their object, and result in a direct and substantial obstruction to or regulation of that commerce.

This argument is founded upon the assertion that the reason for vesting in Congress the power to regulate commerce was to insure uniformity of regulation against conflicting and discriminating state legislation; and the further assertion that the Constitution guarantees liberty of private contract to the citizen, at least upon commercial subjects, and to that extent the guaranty operates as a limitation on the power of Congress to regulate commerce.

Under this grant of power to Congress, that body, in our judgment, may enact such legislation as shall declare void and prohibit the performance of any contract between individuals or corporations where the natural and direct effect of such a contract will be, when carried out, to directly, and not as a mere incident to other and innocent purposes, regulate to any substantial extent interstate commerce. (And when we speak of interstate we also include in our meaning foreign commerce.) We do not assent to the correctness of the proposition that the constitutional guaranty of liberty to the individual to enter into private contracts limits the power of Congress and prevents it from legislating upon the subject of contracts of the class mentioned.

The power of Congress over this subject seems to us much more important and necessary than the liberty of the citizen to enter into contracts of the nature above mentioned, free from the control of Congress, because the direct results of such contracts might be the regulation of commerce among the states, possibly quite as effectually as if a state had passed a statute of like tenor as the contract.

It is, indeed, urged that to include private contracts of this description within the grant of this power to Congress is to take

from the states their own power over the subject, and to interfere with the liberty of the individual in a manner and to an extent never contemplated by the framers of the Constitution, and not fairly justified by any language used in that instrument. If Congress has not the power to legislate upon the subject of contracts of the kind mentioned, because the constitutional provision as to the liberty of the citizen limits, to that extent, its power to regulate interstate commerce, then it would seem to follow that the several states have that power, although such contracts relate to interstate commerce, and, more or less, regulate it. If neither Congress nor the state legislatures have such power, then we are brought to the somewhat extraordinary position that there is no authority, state or national, which can legislate upon the subject of or prohibit such contracts. This cannot be the case.

If it should be held that Congress has no power and the state legislatures have full and complete authority to thus far regulate interstate commerce by means of their control over private contracts between individuals or corporations, then the legislation of the different states might and probably would differ in regard to the matter, according to what each state might regard as its own particular interest. One state might condemn all kinds of contracts of the class described, while another might permit the making of all them, while still another might permit some and prohibit others, and thus great confusion would ensue, and it would be difficult in many cases to know just what law was applicable to any particular contract regarding and regulating interstate commerce. At the same time contracts might be made between individuals or corporations of such extent and magnitude as to seriously affect commerce among the states. These consequences would seemingly necessarily follow if it were decided that the state legislatures had control over the subject to the extent mentioned.

It is true, so far as we are informed, that no state legislature has heretofore authorized by affirmative legislation the making of contracts upon the matter of interstate commerce of the nature now under discussion. Nor has it, in terms, condemned them. The reason why no state legislation upon the subject has been enacted has probably been because it was supposed to be a sub-

ject over which state legislatures have no jurisdiction. If it should be decided that they have, then the course of legislation of the different states on this subject would probably be as varied as we have already indicated.

But upon the matter of interstate and foreign commerce and the proper regulation thereof, the subject being not alone national but international in its character, the great importance of having but one source for the law which regulates that commerce throughout the length and breadth of the land cannot, in our opinion, be overestimated. Each state in that event would have complete jurisdiction over the commerce which was wholly within its own borders, while the jurisdiction of Congress, under the provisions of the Constitution, over interstate commerce would be paramount, and would include therein jurisdiction over contracts of the nature we have been discussing.

We conclude that the plain language of the grant to Congress of power to regulate commerce among the several states includes power to legislate upon the subject of those contracts in respect to interstate or foreign commerce which directly affect and regulate that commerce, and we can find no reasonable ground for asserting that the constitutional provision as to the liberty of the individual limits the extent of that power, as claimed by the appellants. We therefore think the appellants have failed in their contention upon this branch of the subject.

We are thus brought to the question whether the contract or combination proved in this case is one which is either a direct restraint or a regulation of commerce among the several states or with foreign nations contrary to the act of Congress. It is objected on the part of the appellants that even if it affected interstate commerce the contract or combination was only a reasonable restraint upon a ruinous competition among themselves, and was formed only for the purpose of protecting the parties thereto in securing prices for their product that were fair and reasonable to themselves and the public. It is further objected that the agreement does not come within the act because it is not one which amounts to a regulation of interstate commerce, as it has no direct bearing upon or relation to that commerce, but that, on the contrary, the case herein involves

the same principles which were under consideration in *United States* v. *E. C. Knight Co.*,[1] and, in accordance with that decision, the bill should be dismissed.

Referring to the first of these objections to the maintenance of this proceeding, we are of opinion that the agreement or combination was not one which simply secured for its members fair and reasonable prices for the article dealt in by them. Even if the objection thus set up would, if well founded in fact, constitute a defense, we agree with the circuit court of appeals in its statement of the special facts upon this branch of the case and with its opinion thereon as set forth by Circuit Judge Taft, as follows:

The defendants, being manufacturers and vendors of cast-iron pipe, entered into a combination to raise the prices for pipe for all the states west and south of New York, Pennsylvania, and Virginia, constituting considerably more than three quarters of the territory of the United States and significantly called by the associates "pay" territory. Their joint annual output was 220,000 tons. The total capacity of all the other cast-iron pipe manufacturers in the pay territory was 170,500 tons. Of this, 45,000 tons was the capacity of mills in Texas, Colorado, and Oregon, so far removed from that part of the pay territory where the demand was considerable that necessary freight rates excluded them from the possibility of competing, and 12,000 tons was the possible annual capacity of a mill at St. Louis, which was practically under the same management as that of one of the defendants' mills. Of the remainder of the mills in pay territory and outside of the combination, one was at Columbus, Ohio, two in northern Ohio, and one in Michigan. Their aggregate possible annual capacity was about one half the usual annual output of the defendants' mills. They were, it will be observed, at the extreme northern end of the pay territory, while the defendants' mills at Cincinnati, Louisville, Chattanooga and South Pittsburg, and Anniston and Bessemer were grouped much nearer to the center of the pay territory. The freight upon cast-iron pipe amounts to a considerable percentage of the price at which manufacturers can deliver it at any great distance from the place of manufacture. Within the margin of the freight per ton which eastern manufacturers would have to pay to deliver pipe in pay territory the defendants, by controlling two thirds of the output in pay territory, were practically able to fix prices. The competition of the Ohio and

[1] P. 506, *supra*.

Michigan mills of course somewhat affected their power in this respect in the northern part of the pay territory, but the farther south the place of delivery was to be, the more complete the monopoly over the trade which the defendants were able to exercise within the limits already described. Much evidence is adduced upon affidavit to prove that defendants had no power arbitrarily to fix prices and that they were always obliged to meet competition. To the extent that they could not impose prices on the public in excess of the cost price of pipe with freight from the Atlantic seaboard added this is true, but within that limit they could fix prices as they chose. The most cogent evidence that they had this power is the fact everywhere apparent in the record that they exercised it. The details of the way in which it was maintained are somewhat obscured by the manner in which the proof was adduced in the court below, upon affidavits solely and without the clarifying effect of cross-examination, but quite enough appears to leave no doubt of the ultimate fact.

The defendants were by their combination therefore able to deprive the public in a large territory of the advantages otherwise accruing to them from the proximity of defendants' pipe factories, and, by keeping prices just low enough to prevent competition by eastern manufacturers, to compel the public to pay an increase over what the price would have been if fixed by competition between the defendants, nearly equal to the advantage in freight rates enjoyed by defendants over eastern competitors. The defendants acquired this power by voluntarily agreeing to sell only at prices fixed by their committee, and by allowing the highest bidder at the secret auction pool to become the lowest bidder of them at the public letting. Now the restraint thus imposed on themselves was only partial, it did not cover the United States, there was not a complete monopoly. It was tempered by the fear of competition and it affected only a part of the price. But this certainly does not take the contract of association out of the annulling effect of the rule against monopolies. In *United States* v. *E. C. Knight Co.*, 156 U. S. 1, 16, 39 L. ed. 325, 330, 15 Sup. Ct. Rep. 249, Chief Justice Fuller, in speaking for the court, said: "Again, all the authorities agree that in order to vitiate a contract or combination it is not essential that its result should be a complete monopoly; it is sufficient if it really tends to that end and to deprive the public of the advantages which flow from free competition."

It has been earnestly pressed upon us that the prices at which the cast-iron pipe was sold in pay territory were reasonable. A great many affidavits of purchasers of pipe in pay territory, all drawn by the

same hand or from the same model, are produced, in which the affiants say that in their opinion the prices at which pipe has been sold by the defendants have been reasonable. We do not think the issue an important one, because, as already stated, we do not think that at common law there is any question of reasonableness open to the courts with reference to such a contract. Its tendency was certainly to give to the defendants the power to charge unreasonable prices, had they chosen to do so. But if it were important we should unhesitatingly find that the prices charged in the instances which were in evidence were unreasonable. The letters from the manager of the Chattanooga foundry, written to the other defendants and discussing the prices fixed by the association, do not leave the slightest doubt upon this point, and outweigh the perfunctory affidavits produced by the defendants. The cost of producing pipe at Chattanooga, together with a reasonable profit, did not exceed $15 a ton. It could have been delivered at Atlanta at $17 to $18 a ton, and yet the lowest price which that foundry was permitted by the rules of the association to bid was $24.25. The same thing was true all through pay territory to a greater or less degree, and especially at reserved cities.

54 U. S. App. 723, 85 Fed. Rep. 271, 29 C. C. A. 141, 46 L. R. A. 122.

The facts thus set forth show conclusively that the effect of the combination was to enhance prices beyond a sum which was reasonable, and therefore the first objection above set forth need not be further noticed.

We are also of the opinion that the direct effect of the agreement or combination is to regulate interstate commerce, and the case is therefore not covered by that of *United States* v. *E. C. Knight Co.*, 156 U. S. 1, 36 L. ed. 325, 15 Sup. Ct. Rep. 249. It was there held that although the American Sugar Refining Company, by means of the combination referred to, had obtained a practical monopoly of the business of manufacturing sugar, yet the act of Congress did not touch the case, because the combination only related to manufacture, and not to commerce among the states or with foreign nations. The plain distinction between manufacture and commerce was pointed out, and it was observed that a contract or combination which directly related to manufacture only was not brought within the purview of the act, although, as an indirect and incidental

result of such combination, commerce among the states might be thereafter somewhat affected. Mr. Chief Justice Fuller, in delivering the opinion of the court, spoke of the distinction between the two subjects, and said:

The argument is that the power to control the manufacture of refined sugar is a monopoly over a necessity of life, to the enjoyment of which by a large part of the population of the United States interstate commerce is indispensable, and that therefore the general government, in the exercise of the power to regulate commerce, may repress such monopoly directly and set aside the instruments which have created it.

Doubtless, the power to control the manufacture of a given thing involves in a certain sense the control of its disposition, but this is a secondary and not the primary sense; and although the exercise of that power may result in bringing the operation of commerce into play, it does not control it, and affects it only incidentally and indirectly. Commerce succeeds to manufacture and is not a part of it.

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It will be perceived how far-reaching the proposition is that the power of dealing with a monopoly directly may be exercised by the general government whenever interstate or international commerce may be ultimately affected. The regulation of commerce applies to the subjects of commerce, and not to matters of internal police. Contracts to buy, sell, or exchange goods to be transported among the several states, the transportation and its instrumentalities, and articles bought, sold, or exchanged for the purposes of such transit among the states, or put in the way of transit, may be regulated, but this is because they form part of interstate trade or commerce. The fact that an article is manufactured for export to another state does not of itself make it an article of interstate commerce, and the intent of the manufacturer does not determine the time when the article or product passes from the control of the state and belongs to commerce.

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There was nothing in the proofs to indicate any intention to put a restraint upon trade or commerce, and the fact, as we have seen, that trade or commerce might be indirectly affected, was not enough to entitle complainants to a decree.

The direct purpose of the combination in the *Knight Case* was the control of the manufacture of sugar. There was no

combination or agreement, in terms, regarding the future disposition of the manufactured article; nothing looking to a transaction in the nature of interstate commerce. The probable intention on the part of the manufacturer of the sugar to thereafter dispose of it by sending it to some market in another state was held to be immaterial and not to alter the character of the combination. The various cases which had been decided in this court relating to the subject of interstate commerce, and to the difference between that and the manufacture of commodities, and also the police power of the states as affected by the commerce clause of the Constitution, were adverted to, and the case was decided upon the principle that a combination simply to control manufacture was not a violation of the act of Congress, because such a contract or combination did not directly control or affect interstate commerce, but that contracts for the sale and transportation to other states of specific articles were proper subjects for regulation because they did form part of such commerce.

We think the case now before us involves contracts of the nature last above mentioned, not incidentally or collaterally, but as a direct and immediate result of the combination engaged in by the defendants.

While no particular contract regarding the furnishing of pipe and the price for which it should be furnished was in the contemplation of the parties to the combination at the time of its formation, yet it was their intention, as it was the purpose of the combination, to directly and by means of such combination increase the price for which all contracts for the delivery of pipe within the territory above described should be made, and the latter result was to be achieved by abolishing all competition between the parties to the combination. The direct and immediate result of the combination was therefore necessarily a restraint upon interstate commerce in respect of articles manufactured by any of the parties to it to be transported beyond the state in which they were made. The defendants by reason of this combination and agreement could only send their goods out of the state in which they were manufactured for sale and delivery in another state, upon the terms and pursuant to the

provisions of such combination. As pertinently asked by the court below, Was not this a direct restraint upon interstate commerce in those goods?

If dealers in any commodity agreed among themselves that any particular territory bounded by straight lines should be furnished with such commodity by certain members only of the combination, and the others would abstain from business in that territory, would not such agreement be regarded as one in restraint of interstate trade? If the price of the commodity were thereby enhanced (as it naturally would be), the character of the agreement would be still more clearly one in restraint of trade. Is there any substantial difference where by agreement among themselves the parties choose one of their number to make a bid for the supply of the pipe for delivery in another state, and agree that all other bids shall be for a larger sum, thus practically restricting all but the member agreed upon from any attempt to supply the demand for the pipe or to enter into competition for the business? Does not an agreement or combination of that kind restrain interstate trade, and when Congress has acted by the passage of a statute like the one under consideration, does not such a contract clearly violate that statute?

As has frequently been said, interstate commerce consists of intercourse and traffic between the citizens or inhabitants of different states, and includes not only the transportation of persons and property and the navigation of public waters for that purpose, but also the purchase, sale, and exchange of commodities. If, therefore, an agreement or combination directly restrains not alone the manufacture, but the purchase, sale, or exchange of the manufactured commodity among the several states, it is brought within the provisions of the statute. The power to regulate such commerce, that is, the power to prescribe the rules by which it shall be governed, is vested in Congress, and when Congress has enacted a statute such as the one in question, any agreement or combination which directly operates, not alone upon the manufacture, but upon the sale, transportation, and delivery of an article of interstate commerce, by preventing or restricting its sale, etc., thereby regulates inter-

state commerce to that extent, and to the same extent trenches upon the power of the national legislature and violates the statute. We think it plain that this contract or combination effects that result.

The defendants allege, and it is true, that their business is not like a factory manufacturing an article of a certain kind for which there is at all times a demand, and which is manufactured without any regard to a particular sale or for a particular customer. In this respect as in many others the business differs radically from the sugar refiners. The business of defendants is carried on by obtaining particular contracts for the sale, transportation, and delivery of iron pipe of a certain description, quality, and strength, differing in different contracts as the intended use may differ. These contracts are, generally speaking, obtained at a public letting, at which there are many competitors, and the contract bid for includes, in its terms, the sale of the pipe, and its delivery at the place desired, the cost of transportation being included in the purchase price of the pipe. The contract is one for the sale and delivery of a certain kind of pipe, and it is not generally essential to its performance that it should be manufactured for that particular contract, although sometimes it may be.

If the successful bidder had on hand iron pipe of the kind specified, or if he could procure it by purchase, he could in most cases deliver such pipe in fulfillment of his contract just the same as if he manufactured the pipe subsequently to the making of the contract and for the specific purpose of its performance. It is the sale and delivery of a certain kind and quality of pipe, and not the manufacture, which is the material portion of the contract, and a sale for delivery beyond the state makes the transaction a part of interstate commerce. Municipal corporations and gas, railroad, and water companies are among the chief customers for the pipe, and when they desire the article they give notice of the kind and quality, size, strength, and purpose for which the pipe is desired, and announce they will receive proposals for furnishing the same at the place indicated by them. Into this contest (and irrespective of the reserved cities) the defendants enter, not in truth as

competitors, but under an agreement or combination among themselves which eliminates all competition between them for the contract, and permits one of their number to make his own bid and requires the others to bid over him. In certain sections of the country the defendants would have, by reason of their situation, such an advantage over all other competitors that there would practically be no chance for any other than one of their number to obtain the contract, unless the price bid was so exorbitant as to give others not so favorably situated an opportunity to snatch it from their hands. Under these circumstances, the agreement or combination of the defendants, entered into for that express purpose and to directly obtain that desired result, would inevitably and necessarily give to the defendant, who was agreed upon among themselves to make the lowest bid, the contract desired and at a higher price than otherwise would have been obtained, and all the other parties to the combination would, by virtue of its terms, be restricted from an attempt to obtain the contract.

The combination thus had a direct, immediate, and intended relation to and effect upon the subsequent contract to sell and deliver the pipe. It was to obtain that particular and specific result that the combination was formed, and but for the restriction the resulting high prices for the pipe would not have been obtained. It is useless for the defendants to say they did not intend to regulate or affect interstate commerce. They intended to make the very combination and agreement which they in fact did make, and they must be held to have intended (if in such case intention is of the least importance) the necessary and direct result of their agreement.

It is also urged that as but one contract would be awarded for the work proposed at any place, and therefore only one person would secure it by virtue of being the lowest bidder, the selection by defendants of one of their number to make the lowest bid as among themselves could not operate as any restraint of trade; that the combination or agreement operated only to make a selection of that one who should have the contract by being the lowest bidder, and it did not in the most remote degree itself limit the number or extent of contracts, and

therefore could not operate to restrain interstate trade. This takes no heed of the purpose and effect of the combination to restrain the action of the parties to it so that there shall be no competition among them to obtain the contract for themselves.

We have no doubt that where the direct and immediate effect of a contract or combination among particular dealers in a commodity is to destroy competition between them and others, so that the parties to the contract or combination may obtain increased prices for themselves, such contract or combination amounts to a restraint of trade in the commodity, even though contracts to buy such commodity at the enhanced price are continually being made. Total suppression of the trade in the commodity is not necessary in order to render the combination one in restraint of trade. It is the effect of the combination in limiting and restricting the right of each of the members to transact business in the ordinary way, as well as its effect upon the volume or extent of the dealing in the commodity, that is regarded. All the facts and circumstances are, however, to be considered in order to determine the fundamental question — whether the necessary effect of the combination is to restrain interstate commerce.

If iron pipe cost $100 a ton instead of the prices which the record shows were paid for it, no one, we think, would contend that the trade in it would amount to as much as if the lower prices prevailed. The higher price would operate as a direct restraint upon the trade, and therefore any contract or combination which enhanced the price might in some degree restrain the trade in the article. It is not material that the combination did not prevent the letting of any particular contract. Such was not its purpose. On the contrary, the more contracts to be let, the better for the combination. It was formed not for the object of preventing the letting of contracts, but to restrain the parties to it from competing for contracts, and thereby to enhance the prices to be obtained for the pipe dealt in by those parties. And when by reason of the combination a particular contract may have been obtained for one of the parties thereto, but at a higher price than would otherwise have been paid, the charge that the combination was one in restraint of trade is not an-

swered by the statement that the particular contract was in truth obtained and not prevented. The parties to such a combination might realize more profit by the higher prices they would secure than they could earn by doing more work at a much less price. The question is as to the effect of such combination upon the trade in the article, and if that effect be to destroy competition and thus advance the price, the combination is one in restraint of trade.

It is almost needless to add that we do not hold that every private enterprise which may be carried on chiefly or in part by means of interstate shipments is therefore to be regarded as so related to interstate commerce as to come within the regulating power of Congress. Such enterprises may be of the same nature as the manufacturing of refined sugar in the *Knight Case* — that is, the parties may be engaged as manufacturers of a commodity which they thereafter intend at some time to sell, and possibly to sell in another state; but such sale we have already held is an incident to and not the direct result of the manufacture, and so is not a regulation of or an illegal interference with interstate commerce. That principal is not affected by anything herein decided.

The views above expressed lead generally to an affirmance of the judgment of the court of appeals.

OTHER EARLY CASES[1]

HOPKINS *v.* UNITED STATES

(171 U. S. 578; Supreme Court, October 24, 1898; Opin., Peckham, J.)

This was a bill in equity, filed by direction of the Attorney-General, against Hopkins and other members of the Kansas City Live Stock Exchange, to secure a dissolution of the exchange on the ground that its members were in a combination in restraint of commerce among the several states.

[1] Reply of the Attorney-General to a communication from the Hon. George F. Hoar, Chairman of the Committee on the Judiciary of the United States Senate, Jan. 3, 1903.

It seems that this exchange was an association of men doing business at the stock yards in Kansas City, part of these yards being in Missouri and part in Kansas. The business of the members was to receive live stock shipped from other states, care for and sell the same, and account to the owners for the proceeds after deducting charges and expenses. Under the rules, members were prohibited from buying live stock from commission merchants in Kansas City not members of the exchange. The rules also fixed a commission, prohibited the employment of agents to solicit consignments except upon stipulated salary, and forbade the sending of prepaid telegrams or telephone messages with information as to the condition of the markets.

The Court held that the business conducted by the members of the exchange was not interstate, but local in character, and therefore decided the case against the government.

Page 588:

The sale or purchase of live stock as commission merchants at Kansas City is the business done, and its character is not altered because the larger proportion of the purchases and sales may be of live stock sent into the state from other states or from the territories. Where the stock came from or where it may ultimately go after a sale or purchase, procured through the services of one of the defendants at the Kansas City stock yards, is not the substantial factor in the case. The character of the business of defendants must, in this case, be determined by the facts occurring at that city.

If an owner of cattle in Nebraska accompanied them to Kansas City and there personally employed one of these defendants to sell the cattle at the stock yards for him on commission, could it be properly said that such defendant, in conducting the sale for his principal, was engaged in interstate commerce? Or that an agreement between himself and others not to render such services for less than a certain sum was a contract in restraint of interstate trade or commerce? We think not. On the contrary, we regard the services as collateral to such commerce and in the nature of a local aid or facility provided for the cattle owner toward the accomplishment of his purpose to sell them, and an agreement among those who render the services relating to the terms upon which they will render them is not a contract in restraint of interstate trade or commerce.

Page 590:

The selling of an article at its destination, which has been sent from another state, while it may be regarded as an interstate sale and one which the importer was entitled to make, yet the services of the individual employed at the place where the article is sold are not so connected with the subject sold as to make them a portion of interstate commerce, and a combination in regard to the amount to be charged for such service is not, therefore, a combination in restraint of that trade or commerce. Granting that the cattle themselves, because coming from another state, are articles of interstate commerce, yet it does not therefore follow that before their sale all persons performing services in any way connected with them are themselves engaged in that commerce, or that their agreements among each other relative to the compensation to be charged for their services are void as agreements made in restraint of interstate trade.

Page 592:

The contract condemned by the statute is one whose direct and immediate effect is a restraint upon that kind of trade or commerce which is interstate. Charges for such facilities as we have already mentioned are not a restraint upon that trade, although the total cost of marketing a subject thereof may be thereby increased. Charges for facilities furnished have been held not a regulation of commerce, even when made for services rendered or as compensation for benefits conferred.

Anderson *v.* United States

(171 U. S. 604; Supreme Court, October 24, 1898; Opin., Peckham, J.)

This case was somewhat similar to the Hopkins case, being a bill in equity filed by direction of the Attorney-General against the members of the Traders' Live Stock Exchange of Kansas City to compel its dissolution. The main difference between this exchange and that involved in the Hopkins case was that while the members of the Traders' Exchange were purchasers of live stock on the market, the members of the Live Stock Exchange were only commission merchants who sold the live stock upon commission as a compensation for their services.

The rules of the exchange relied upon by the government as

restraining interstate commerce were those which forbade the recognition of any yard trader unless he was a member of the exchange, which required all the members of a partnership to be members of the exchange, which provided that no member of the exchange should employ any person to buy or sell cattle unless such person was a member of the exchange, and which prohibited the payment of any fee to any buyer or salesman for buying cattle from or selling cattle to such party.

Without passing upon the question whether the members of this exchange were or were not engaged in interstate commerce, the Court held that the rules objected to were of a character to enforce the purpose and object of the exchange, and viewed in that light were reasonable and fair. They could affect interstate trade or commerce in but a remote way, and therefore could not be regarded as in restraint of such trade or commerce.

The Court (page 615) restated the rule that where the subject matter of the agreement does not directly relate to and act upon and embrace interstate commerce, and where the undisputed facts clearly show that the purpose of the agreement was not to regulate, obstruct, or restrain that commerce, but that it was entered into with the object of properly and fairly regulating the transaction of the business in which the parties to the agreement were engaged, such agreement would be upheld as not within the statute.

A few minor Supreme Court cases under the Harrison, Cleveland, and McKinley administrations may be dismissed even more briefly. The Greenhut proceedings of 1892 were directed against the Whisky Trust but proved abortive. The cash register combination [Chapter XVIII, *infra*] was indicted; but the case was allowed to lapse "because of reconciliation of complaining witness with defendants." In other words, the independents were merged with the combination. There were several labor decisions; such as the Debs cases which arose out of the great railway strike at Chicago in 1894. Several local coal dealers' associations were proceeded against. But except for the opinions outlined in this and the preceding chapter, they played no part in the unfolding of a public policy toward industrial monopoly. — ED.

XVII

DEFINITIVE ANTI-TRUST LAW INTERPRETATION

1901–1911

It would be futile, if not confusing, even to outline all of the Federal court decisions which during a decade led up to the great Standard Oil opinion of 1911. The great activity of the Federal Department of Justice under Presidents Roosevelt and Taft has already been described.[1] All that need be done is to classify these decisions according to the nature of the defendants. For however positive in their repressive effects, none of these judgments contributed to any real development of the law. Even the Northern Securities case,[2] aside from its bearing upon the device of the holding company and upon the constitutional question of states' rights, only disclosed the conflict of opinion as to the regulation of monopoly in the mind of the court. It is interesting, nevertheless, to group the numerous proceedings, even if they fail to mark any real turning points in legal construction.

The great staple monopolies are represented, aside from the petroleum, tobacco, steel, and harvester companies herein described in full, by repeated attacks upon the beef trust, the sugar refining combination and the gunpowder monopoly. The first beef prosecutions were directed against the Swifts in 1902, followed three years later by prosecutions against Armour & Co. It was in the latter that the issue really became one of procedure in obtaining evidence. For without competent witnesses, namely those really connected with the business, little progress was possible. The involved mass of technicalities led up to the "immunity bath" decision and statutes, which are primarily of importance to the specialist.[3] As for the sugar trust, its fate still hangs in the balance. The explosives combination was attacked in 1907, and four years later was ordered dissolved by decree of the Supreme Court of the United States.[4] The glucose combination in the person of the Corn Products Company is just now on trial for its life. Next in popular interest, probably, come the cases in transportation, already outlined in chapter XV as to railroads ; the water carriers were dealt with by proceedings against agreements in the South American, Oriental and Alaskan carrying trades, against

[1] P. 490, *supra*. [2] P. 491, *supra*.

[3] Details in Ripley, Railroads: Rates and Regulation, p. 550.

[4] An admirable account of this combination is in *Quarterly Journal of Economics*, Vol. XXVI, 1912, pp. 444–481, and of its dissolution in *Idem*, XXVII, 1912, p. 202 ff.

tow boat combinations on the Great Lakes, and steerage pools in the European service. A third distinct group of prosecutions dealt with attempted temporary corners in such staples as coffee, grain, and cotton, exemplified in the Sielcken valorization case of 1912, the Patten and Thompson convictions of 1910 and 1913, and the Chicago Board of Trade proceedings. Dealings with public utilities corporations are relatively few. The amicable settlement with the American Telephone and Telegraph Company in 1914 is a rare exception. Apart from the railroads, most public utilities are subject, if at all, to the control of the several states.

A large group of the anti-trust prosecutions during the decade after 1901, were directed against local and sometimes petty attempts at the elimination of competition in merchandising.[1] Jobbers' and retailers' agreements in the lumber trade were perhaps the most frequent, with coal cases as a close second. Wholesale grocers' associations, particularly in the South; agreements between dealers in such necessities as ice, milk and butter; attempts by pooling or otherwise to enhance prices of fruit and produce, naval stores, wall paper, plumbing supplies, drugs, and even charcoal and kindling wood; combinations between jewelry manufacturers and bill posters; periodical and newspaper "insides" clearing houses; even such apparently free businesses as quarrying and deep-sea fishing; all these have been haled into court with varying degrees of success to the government. Most of these were pools or price agreements of one sort or another, and are best described by reference to the preceding chapters, (I) dealing with the early salt association, (III) the more recent wire nail pool, or (IV) the Addystone pipe combination.[2] Of distinctively labor decisions, there were many; although none rivaled the Debs case of 1894 in importance. Fines were imposed upon seventy-two Louisiana laborers in 1908. Joe Cotton and others were indicted for a strike on the Illinois Central; and an alleged conspiracy among longshoremen was attacked three years later. In 1913 the United Mine Workers' and the electricians' unions were proceeded against. And the noteworthy and tragic conviction of the hatters' national union after protracted litigation, in *Loewe* v. *Lawlor*, with fines aggregating a quarter of a million dollars exercised a great influence upon the Federal legislation of 1914 amending the Sherman Anti-Trust law [Chapter XIX, *infra*]. And then, more rarely, there are the efforts to control association in their own interest by agriculturists, — the more notable, perhaps, because of the agitation for and subsequent amendment by the Clayton bill in 1914, exempting farmers from the Anti-Trust law altogether. The case of *United States* v. *Steers* in 1910, seeking to restrain the Kentucky "Night Riders" from regulating production in the Burley tobacco fields, led to the conviction of, and imposition of fines aggregating $3500 upon, eight

[1] Details by Stevens in *Quarterly Journal of Economics*, Vol. XXVI, 1912, pp. 630 ff.

[2] *Cf.* also *Quarterly Journal of Economics*, Vol. XXVI, 1912, pp. 593–643, and *American Economic Review*, 1913, pp. 549–575.

of the ring leaders. The prosecution of the butter and egg combinations of Chicago and Elgin, Illinois, in 1912–1914 belongs rather in the category of merchandising than of agricultural production.

Two other distinct groups of cases deal, respectively, with abuse of the privilege of Federal licenses — the so-called patent pools — and with vicious trade practices, as such, irrespective of the nature of the combination. These will be exemplified concretely in the decisions reported in the next chapter, which were framed upon the basis of the construction according to the law of reason in the Standard Oil decision. There were many of each of these during the decade to 1911 under review; but they in no instance attained prominence because of any advance in the interpretation of the anti-monopoly law.[1] This distinction was reserved for the two leading opinions reprinted in this chapter. They mark a sharp turning point in construction,[2] the entire conviction at last of the mind of the Supreme Court of the United States, that all was not well with business as it had come to be conducted in America, but that, nevertheless, the time had arrived to discriminate between what was evil, deserving elimination, and that which was so inherently sound and necessary as to merit the protection, nay even the encouragement, of the law. The legal basis for this distinction is outlined in the following opinions. — ED.

THE STANDARD OIL DECISION[3]

Mr. Chief Justice White delivered the opinion of the court.

The conspiracy was alleged to have been formed in or about the year 1870 by three of the individual defendants, viz.: John D. Rockefeller, William Rockefeller, and Henry M. Flagler. The detailed averments concerning the alleged conspiracy were ar-

[1] Possible exception may be made of *Montague & Company* v. *Lowry*. (193 U. S. Rep. 38. Decided February 23, 1904.) An association was formed in California by manufacturers of and dealers in tiles, mantels, and grates; the dealers agreed not to purchase materials from manufacturers who were not members, and not to sell unset tiles for less than list prices, which were 50 per cent higher than to members. Manufacturers, resident in other states than California, agreed not to sell to any other than members. Membership was prescribed by rules, such as carrying $3000 worth of stock. A firm of outside dealers who were not members, and who did not carry $3000 worth of stock, brought action under § 7 of the Anti-Trust Act of 1890. It was held, that although sales within the state were but a small part of the total transactions involved, the general effect of the scheme was to enhance prices; and that it was impossible to separate intrastate from interstate business; and that a combination in restraint of trade had been shown. The parties aggrieved were entitled to recover threefold damages as found by the jury.

[2] On this point *cf. Journal of Political Economy*, Vol. XXIII, 1915, pp. 204 ff.

[3] *Standard Oil Co.* v. *United States*, 31 Supreme Court Reporter, 502; 221 U. S. 1. Decided May 15, 1911. Many extended legal citations are stricken out for purposes

ranged with reference to three periods, the first from 1870 to 1882, the second from 1882 to 1899, and the third from 1899 to the time of the filing of the bill.

The general charge concerning the period from 1870 to 1882 was as follows:

> That during said first period the said individual defendants, in connection with the Standard Oil Company of Ohio, purchased and obtained interests through stock ownership and otherwise in, and entered into agreements with, various persons, firms, corporations, and limited partnerships engaged in purchasing, shipping, refining, and selling petroleum and its products among the various states, for the purpose of fixing the price of crude and refined oil and the products thereof, limiting the production thereof, and controlling the transportation therein, and thereby restraining trade and commerce among the several states, and monopolizing the said commerce.

To establish this charge it was averred that John D. and William Rockefeller and several other named individuals, who, prior to 1870, composed three separate partnerships engaged in the business of refining crude oil and shipping its products in interstate commerce, organized in the year 1870 a corporation known as the Standard Oil Company of Ohio, and transferred to that company the business of the said partnerships, the members thereof becoming, in proportion to their prior ownership, stockholders in the corporation. It was averred that the other individual defendants soon afterwards became participants in the illegal combination, and either transferred property to the corporation or to individuals, to be held for the benefit of all parties in interest in proportion to their respective interests in the combination; that is, in proportion to their stock ownership in the Standard Oil Company of Ohio. By the means thus stated, it was charged that by the year 1872, the combination had acquired substantially all but three or four of the thirty-five or forty oil refineries located in Cleveland, Ohio. By reason of the power thus obtained, and in further execution of the intent

of condensation, where merely cross references, often without specific indication. This is a compilation for economists, not for lawyers. An excellent commentary by Professor Seager will be found in *Political Science Quarterly*, Vol. XXVI, 1911, pp. 581–614.

and purpose to restrain trade and to monopolize the commerce, interstate as well as intrastate, in petroleum and its products, the bill alleged that the combination and its members obtained large preferential rates and rebates in many and devious ways over their competitors from various railroad companies, and that by means of the advantage thus obtained many, if not virtually all, competitors were forced either to become members of the combination or were driven out of business; and thus, it was alleged, during the period in question, the following results were brought about: (*a*) That the combination, in addition to the refineries in Cleveland which it had acquired, as previously stated, and which it had either dismantled to limit production, or continued to operate, also from time to time acquired a large number of refineries of crude petroleum, situated in New York, Pennsylvania, Ohio, and elsewhere. The properties thus acquired, like those previously obtained, although belonging to and being held for the benefit of the combination, were ostensibly divergently controlled, some of them being put in the name of the Standard Oil Company of Ohio, some in the name of corporations or limited partnerships affiliated therewith, or some being left in the name of the original owners, who had become stockholders in the Standard Oil Company of Ohio, and thus members of the alleged illegal combination. (*b*) That the combination had obtained control of the pipe lines available for transporting oil from the oil fields to the refineries in Cleveland, Pittsburg, Titusville, Philadelphia, New York, and New Jersey. (*c*) That the combination during the period named had obtained a complete mastery over the oil industry, controlling 90 per cent of the business of producing, shipping, refining, and selling petroleum and its products, and thus was able to fix the price of crude and refined petroleum, and to restrain and monopolize all interstate commerce in those products.

The averments bearing upon the second period (1882 to 1899) had relation to the claim:

That during the said second period of conspiracy the defendants entered into a contract and trust agreement, by which various independent firms, corporations, limited partnerships, and individuals engaged in purchasing, transporting, refining, shipping, and selling

oil and the products thereof among the various states, turned over the management of their said business, corporations, and limited partnerships to nine trustees, composed chiefly of certain individuals defendant herein, which said trust agreement was in restraint of trade and commerce, and in violation of law, as hereinafter more particularly alleged.

The trust agreement thus referred to was set out in the bill. It was made in January, 1882. By its terms the stock of forty corporations, including the Standard Oil Company of Ohio, and a large quantity of various properties which had been previously acquired by the alleged combination, and which was held in diverse forms, as we have previously indicated, for the benefit of the members of the combination, was vested in the trustees and their successors, "to be held for all parties in interest jointly." In the body of the trust agreement was contained a list of the various individuals and corporations and limited partnerships whose stockholders and members, or a portion thereof, became parties to the agreement. This list is in the margin. [Omitted.]

The agreement made provision for the method of controlling and managing the property by the trustees, for the formation of additional manufacturing, etc., corporations in various states, and the trust, unless terminated by a mode specified, was to continue "during the lives of the survivors and survivor of the trustees named in the agreement and for twenty-one years thereafter." The agreement provided for the issue of Standard Oil Trust certificates to represent the interest arising under the trust in the properties affected by the trust, which, of course, in view of the provisions of the agreement and the subject to which it related caused the interest in the certificates to be coincident with and the exact representative of the interest in the combination, that is, in the Standard Oil Company of Ohio. Soon afterwards it was alleged the trustees organized the Standard Oil Company of New Jersey and the Standard Oil Company of New York, the former having a capital stock of $3,000,000 and the latter a capital stock of $5,000,000, subsequently increased to $10,000,000, and $15,000,000, respectively. The bill alleged "that pursuant to said trust agreement the said trustees caused to be transferred to themselves the stocks of all corporations and limited partnerships named in said trust agreement, and caused various of the

individuals and copartnerships who owned apparently independent refineries and other properties employed in the business of refining and transporting and selling oil in and among said various states and territories of the United States, as aforesaid, to transfer their property situated in said several states to the respective Standard Oil Companies of said States of New York, New Jersey, Pennsylvania, and Ohio, and other corporations organized or acquired by said trustees from time to time. . . ." For the stocks and property so acquired the trustees issued trust certificates. It was alleged that in 1888 the trustees "unlawfully controlled the stock and ownership of various corporations and limited partnerships engaged in such purchase and transportation, refining, selling, and shipping of oil," as per a list which is excerpted in the margin. [List omitted.]

The bill charged that during the second period quo warranto proceedings were commenced against the Standard Oil Company of Ohio, which resulted in the entry by the supreme court of Ohio, on March 2, 1892, of a decree adjudging the trust agreement to be void, not only because the Standard Oil Company of Ohio was a party to the same, but also because the agreement in and of itself was in restraint of trade and amounted to the creation of an unlawful monopoly. It was alleged that shortly after this decision, seemingly for the purpose of complying therewith, voluntary proceedings were had apparently to dissolve the trust, but that these proceedings were a subterfuge and a sham because they simply amounted to a transfer of the stock held by the trust in sixty-four of the companies which it controlled to some of the remaining twenty companies, it having controlled before the decree eighty-four in all, thereby, while seemingly in part giving up its dominion, yet in reality preserving the same by means of the control of the companies as to which it had retained complete authority. It was charged that especially was this the case, as the stock in the companies selected for transfer was virtually owned by the nine trustees or the members of their immediate families or associates. The bill further alleged that in 1897 the attorney-general of Ohio instituted contempt proceedings in the quo warranto case, based upon the claim that the trust had not been dissolved as required

by the decree in that case. About the same time, also, proceedings in quo warranto were commenced to forfeit the charter of a pipe line known as the Buckeye Pipe Line Company, an Ohio corporation, whose stock, it was alleged, was owned by the members of the combination, on the ground of its connection with the trust which had been held to be illegal.

The result of these proceedings, the bill charged, caused a resort to the alleged wrongful acts asserted to have been committed during the third period, as follows:

That during the third period of said conspiracy, and in pursuance thereof, the said individual defendants operated through the Standard Oil Company of New Jersey, as a holding corporation, which corporation obtained and acquired the majority of the stocks of the various corporations engaged in purchasing, transporting, refining, shipping, and selling oil into and among the various states and territories of the United States and the District of Columbia and with foreign nations, and thereby managed and controlled the same, in violation of the laws of the United States, as hereinafter more particularly alleged.

It was alleged that in or about the month of January, 1899, the individual defendants caused the charter of the Standard Oil Company of New Jersey to be amended, "so that the business and objects of said company were stated as follows, to wit: 'To do all kinds of mining, manufacturing, and trading business; transporting goods and merchandise by land or water in any manner; to buy, sell, lease, and improve land; build houses, structures, vessels, cars, wharves, docks, and piers; to lay and operate pipe lines; to erect lines for conducting electricity; to enter into and carry out contracts of every kind pertaining to its business; to acquire, use, sell, and grant licenses under patent rights; to purchase or otherwise acquire, hold, sell, assign, and transfer shares of capital stock and bonds or other evidences of indebtedness of corporations, and to exercise all the privileges of ownership, including voting upon the stock so held; to carry on its business and have offices and agencies therefor in all parts of the world, and to hold, purchase, mortgage, and convey real estate and personal property outside the state of New Jersey.'"

The capital stock of the company—which, since March 19,

1892, had been $10,000,000 — was increased to $110,000,000; and the individual defendants, as therefore, continued to be a majority of the board of directors.

Without going into detail it suffices to say that it was alleged in the bill that shortly after these proceedings the trust came to an end, the stock of the various corporations which had been controlled by it being transferred by its holders to the Standard Oil Company of New Jersey, which corporation issued therefor certificates of its common stock to the amount of $97,250,000. The bill contained allegations referring to the development of new oil fields; for example, in California, southeastern Kansas, northern Indian territory, and northern Oklahoma, and made reference to the building or otherwise acquiring by the combination of refineries and pipe lines in the new fields for the purpose of restraining and monopolizing the interstate trade in petroleum and its products.

Reiterating in substance the averments that both the Standard Oil Trust from 1882 to 1899, and the Standard Oil Company of New Jersey, since 1899, had monopolized and restrained interstate commerce in petroleum and its products, the bill at great length additionally set forth various means by which, during the second and third periods, in addition to the effect occasioned by the combination of alleged previously independent concerns, the monopoly and restraint complained of were continued. Without attempting to follow the elaborate averments on these subjects, spread over fifty-seven pages of the printed record, it suffices to say that such averments may properly be grouped under the following heads: Rebates, preferences, and other discriminatory practices in favor of the combination by railroad companies; restraint and monopolization by control of pipe lines, and unfair practices against competing pipe lines; contracts with competitors in restraint of trade; unfair methods of competition, such as local price cutting at the points where necessary to suppress competition; espionage of the business of competitors, the operation of bogus independent companies, and payment of rebates on oil, with the like intent; the division of the United States into districts, and the limiting the operations of the various subsidiary corporations as to such districts so that

competition in the sale of petroleum products between such corporations had been entirely eliminated and destroyed; and finally reference was made to what was alleged to be the "enormous and unreasonable profits" earned by the Standard Oil Trust and the Standard Oil Company as a result of the alleged monopoly; which presumably was averred as a means of reflexly inferring the scope and power acquired by the alleged combination.

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Coming to the prayer of the bill, it suffices to say that in general terms the substantial relief asked was, first, that the combination in restraint of interstate trade and commerce, and which had monopolized the same, as alleged in the bill, be found to have existence, and that the parties thereto be perpetually enjoined from doing any further act to give effect to it; second, that the transfer of the stocks of the various corporations to the Standard Oil Company of New Jersey, as alleged in the bill, be held to be in violation of the 1st and 2d sections of the anti-trust act, and that the Standard Oil Company of New Jersey be enjoined and restrained from in any manner continuing to exert control over the subsidiary corporations by means of ownership of said stock or otherwise; third, that specific relief by injunction be awarded against further violation of the statute by any of the acts specifically complained of in the bill. There was also a prayer for general relief.

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Duly appreciating the situation just stated [directly opposing contentions of counsel], it is certain that only one point of concord between the parties is discernible, which is, that the controversy in every aspect is controlled by a correct conception of the meaning of the 1st and 2d sections of the anti-trust act. We shall therefor — departing from what otherwise would be the natural order of analysis — make this one point of harmony the initial basis of our examination of the contentions, relying upon the conception that by doing so some harmonious resonance may result adequate to dominate and control the discord with which the case abounds. That is to say, we shall first come to consider the meaning of the 1st and 2d sections of the anti-trust act by

the text, and after discerning what by that process appears to be its true meaning, we shall proceed to consider the respective contentions of the parties concerning the act, the strength or weakness of those contentions, as well as the accuracy of the meaning of the act as deduced from the text in the light of the prior decisions of this court concerning it. When we have done this, we shall then approach the facts. Following this course, we shall make our investigation under four separate headings: First. The text of the 1st and 2d sections of the act, originally considered, and its meaning in the light of the common law and the law of this country at the time of its adoption. Second. [P. 571, *infra.*] The contentions of the parties concerning the act, and the scope and effect of the decisions of this court upon which they rely. Third. [P. 577, *infra.*] The application of the statute to facts: and, Fourth. [P. 581, *infra.*] The remedy, if any, to be afforded as the result of such application.

First. The text of the act and its meaning.

We quote the text of the 1st and 2d sections of the act, as follows: [On p. 484, *supra.*]

The debates show that doubt as to whether there was a common law of the United States which governed the subject in the absence of legislation was among the influences leading to the passage of the act. They conclusively show, however, that the main cause which led to the legislation was the thought that it was required by the economic condition of the times; that is, the vast accumulation of wealth in the hands of corporations and individuals, the enormous development of corporate organization, the facility for combination which such organizations afforded, the fact that the facility was being used, and that combinations known as trusts were being multiplied, and the widespread impression that their power had been and would be exerted to oppress individuals and injure the public generally. Although debates may not be used as a means for interpreting a statute, that rule, in the nature of things, is not violated by resorting to debates as a means of ascertaining the environment at the time of the enactment of a particular law; that is, the history of the period when it was adopted.

There can be no doubt that the sole subject with which the 1st

section deals is restraint of trade as therein contemplated, and that the attempt to monopolize and monopolization is the subject with which the 2d section is concerned. It is certain that those terms, at least in their rudimentary meaning, took their origin in the common law, and were also familiar in the law of this country prior to and at the time of the adoption of the act in question.

We shall endeavor then, first, to seek their meaning, not by indulging in an elaborate and learned analysis of the English law and of the law of this country, but by making a very brief reference to the elementary and indisputable conceptions of both the English and American law on the subject prior to the passage of the anti-trust act.

a. It is certain that at a very remote period the words "contract in restraint of trade" in England came to refer to some voluntary restraint put by contract by an individual on his right to carry on his trade or calling. Originally all such contracts were considered to be illegal, because it was deemed they were injurious to the public as well as to the individuals who made them. In the interest of the freedom of individuals to contract, this doctrine was modified so that it was only when a restraint by contract was so general as to be coterminous with the kingdom that it was treated as void. That is to say, if the restraint was partial in its operation, and was otherwise reasonable, the contract was held to be valid:

b. Monopolies were defined by Lord Coke as follows:

> A monopoly is an institution or allowance by the King by his grant, commission, or otherwise, to any person or persons, bodies politic or corporate, of or for the sole buying, selling, making, working, or using of anything, whereby any person or persons, bodies politic or corporate, are sought to be restrained of any freedom or liberty that they had before, or hindered in their lawful trade. (3 Inst. 181.)

Hawkins thus defined them:

> A monopoly is an allowance by the King to a particular person or persons of the sole buying, selling, making, working, or using of anything whereby any person is sought to be restrained from any freedom [of manufacturing or trading] which he had before. (Hawk. P. C. bk. 1, chap. 79.)

The frequent granting of monopolies and the struggle which led to a denial of the power to create them, that is to say, to the establishment that they were incompatible with the English Constitution, is known to all and need not be reviewed.[1] The evils which led to the public outcry against monopolies and to the final denial of the power to make them may be thus summarily stated: (1) The power which the monopoly gave to the one who enjoyed it, to fix the price and thereby injure the public; (2) The power which it engendered of enabling a limitation on production; and (3) The danger of deterioration in quality of the monopolized article which it was deemed was the inevitable resultant of the monopolistic control over its production and sale. As monopoly, as thus conceived, embraced only a consequence arising from an exertion of sovereign power, no express restrictions or prohibitions obtained against the creation by an individual of a monopoly as such. But as it was considered, at least, so far as the necessaries of life were concerned, that individuals, by the abuse of their right to contract, might be able to usurp the power arbitrarily to enhance prices (one of the wrongs arising from monopoly), it came to be that laws were passed relating to offenses such as forestalling, regrating, and engrossing by which prohibitions were placed upon the power of individuals to deal under such circumstances and conditions as, according to the conception of the times, created a presumption that the dealings were not simply the honest exertion of one's right to contract for his own benefit, unaccompanied by a wrongful motive to injure others, but were the consequence of a contract or course of dealing of such a character as to give rise to the presumption of an intent to injure others through the means, for instance, of a monopolistic increase of prices. This is illustrated by the definition of engrossing found in the statue, 5 and 6 Edw. VI., chap. 14, as follows:

Whatsoever person or persons . . . shall engross or get into his or their hands by buying, contracting, or promise-taking, other than by demise, grant, or lease of land, or tithe, any corn growing in the fields, or any other corn or grain, butter, cheese, fish, or other dead victuals

[1] *Cf.* W. H. Price's admirable English Patents of Monopoly, *Harvard Economic Studies*, 1906. — Ed.

whatsoever, within the realm of England, to the intent to sell the same again, shall be accepted, reputed, and taken an unlawful engrosser or engrossers.

As by the statues providing against engrossing the quantity engrossed was not required to be the whole or a proximate part of the whole of an article, it is clear that there was a wide difference between monopoly and engrossing, etc. But as the principal wrong which it was deemed would result from monopoly, that is, an enhancement of the price, was the same wrong to which it was thought the prohibited engrossment would give rise, it came to pass that monopoly and engrossing were regarded as virtually one and the same thing. In other words, the prohibited act of engrossing, because of its inevitable accomplishment of one of the evils deemed to be engendered by monopoly, came to be referred to as being a monopoly or constituting an attempt to monopolize. Thus Pollexfen, in his argument in *East India Co.* v. *Sandys*, Skinner, 165, 169, said:

By common law, he said that trade is free, and for that cited 3 Co. Inst. 181; F. B. 65; *Taylors de Ipswich* v. *Sherring*, 1 Rolle, Rep. 4; that the common law is as much against monopoly as engrossing; and that they differ only that a monopoly is by patent from the King, the other is by the act of the subject between party and party; but that the mischiefs are the same from both, and there is the same law against both. *Darcy* v. *Allen*, F. Moore, 673, 11 Coke, 84. The sole trade of anything is engrossing *ex rei natura*, from whosoever hath the sale trade of buying and selling hath engrossed that trade; and whosoever hath the sole trade to any country hath the sole trade of buying and selling the product of that country, at his own price, which is an engrossing.

And by operation of the mental process which led to considering as a monopoly acts which, although they did not constitute a monopoly, were thought to produce some of its baneful effects, so also because of the impediment or burden to the due course of trade which they produced, such acts came to be referred to as in restraint of trade. This is shown by my Lord Coke's definition of monopoly as being "an institution or allowance . . . whereby any person or persons, bodies politic or corporate, are sought to be restrained of any freedom or liberty

that they had before, or hindered in their lawful trade." It is illustrated also by the definition which Hawkins gives of monopoly wherein it is said that the effect of monopoly is to restrain the citizen "from the freedom of manufacturing or trading which he had before." And see especially the opinion of Parker, C. J., in *Mitchel* v. *Reynolds* (1711), 1 P. Ws. 181 where a classification is made of monopoly which brings it generically within the description of restraint of trade.

Generalizing these considerations, the situation is this: 1. That by the common law, monopolies were unlawful because of their restriction upon individual freedom of contract and their injury to the public. 2. That as to necessaries of life, the freedom of the individual to deal was restricted where the nature and character of the dealing was such as to engender the presumption of intent to bring about at least one of the injuries which it was deemed would result from monopoly, — that is, an undue enhancement of price. 3. That to protect the freedom of contract of the individual, not only in his own interest, but principally in the interest of the common weal, a contract of an individual by which he put an unreasonable restraint upon himself as to carrying on his trade or business was void. And that at common law the evils consequent upon engrossing, etc., caused those things to be treated as coming within monopoly and sometimes to be called monopoly, and the same considerations caused monopoly, because of its operation and effect, to be brought within and spoken of generally as impeding the due course of, or being in restraint of, trade.

From the development of more accurate economic conceptions and the changes in conditions of society, it came to be recognized that the acts prohibited by the engrossing, forestalling, etc., statutes did not have the harmful tendency which they were presumed to have when the legislation concerning them was enacted, and therefore did not justify the presumption which had previously been deduced from them, but, on the contrary, such acts tended to fructify and develop trade. See the statutes of 12th George III, chap. 71, enacted in 1772, and statute of 7 and 8 Victoria, chap. 24, enacted in 1844, repealing the prohibitions against engrossing, forestalling, etc., upon the

express ground that the prohibited acts had come to be considered as favorable to the development of, and not in restraint of, trade. It is remarkable that nowhere at common law can there be found a prohibition against the creation of monopoly by an individual. This would seem to manifest, either consciously or intuitively, a profound conception as to the inevitable operation of economic forces and the equipose or balance in favor of the protection of the rights of individuals which resulted. That is to say, as it was deemed that monopoly in the concrete could only arise from an act of sovereign power, and, such sovereign power being restrained, prohibitions as to individuals were directed not against the creation of monopoly, but were only applied to such acts in relation to particular subjects as to which it was deemed, if not restrained, some of the consequences of monopoly might result. After all, this was but an instinctive recognition of the truisms that the course of trade could not be made free by obstructing it, and that an individual's right to trade could not be protected by destroying such right.

From the review just made it clearly results that outside of the restrictions resulting from the want of power in an individual to voluntarily and unreasonably restrain his right to carry on his trade or business, and outside of the want of right to restrain the free course of trade by contracts or acts which implied a wrongful purpose, freedom to contract and to abstain from contracting, and to exercise every reasonable right incident thereto, became the rule in the English law. The scope and effect of this freedom to trade and contract is clearly shown by the decision in *Mogul S. S. Co.* v. *McGregor* [1891]. While it is true that the decision of the House of Lords in the case in question was announced shortly after the passage of the anti-trust act, it serves reflexly to show the exact state of the law in England at the time the anti-trust statute was enacted.

In this country also the acts from which it was deemed there resulted a part, if not all, of the injurious consequences ascribed to monopoly, came to be referred to as a monopoly itself. In other words, here as had been the case in England, practical common sense caused attention to be concentrated not upon the theoretically correct name to be given to the condition or acts

which gave rise to a harmful result, but to the result itself and to the remedying of the evils which it produced. The statement just made is illustrated by an early statute of the province of Massachusetts, that is, chap. 31 of the Laws of 1778–1779, by which monopoly and forestalling were expressly treated as one and the same thing.

It is also true that while the principles concerning contracts in restraint of trade, that is, voluntary restraint put by a person on his right to pursue his calling, hence only operating subjectively, came generally to be recognized in accordance with the English rule, it came moreover to pass that contracts or acts which it was considered had a monopolistic tendency, especially those which were thought to unduly diminish competition and hence to enhance prices — in other words, to monopolize — came also in a generic sense to be spoken of and treated as they had been in England, as restricting the due course of trade, and therefore as being in restraint of trade. The dread of monopoly as an emanation of governmental power, while it passed at an early date out of mind in this country, as a result of the structure of our government, did not serve to assuage the fear as to the evil consequences which might arise from the acts of individuals producing or tending to produce the consequences of monopoly. It resulted that treating such acts as we have said as amounting to monopoly, sometimes constitutional restrictions, again legislative enactments or judicial decisions, served to enforce and illustrate the purpose to prevent the occurrence of the evils recognized in the mother country as consequent upon monopoly, by providing against contracts or acts of individuals or combinations of individuals or corporations deemed to be conducive to such results. To refer to the constitutional or legislative provisions on the subject, or the many judicial decisions which illustrate it, would unnecessarily prolong this opinion. We append in the margin a note to treaties, etc., wherein are contained references to constitutional and statutory provisions and to numerous decisions, etc., relating to the subject. [Omitted.]

It will be found that, as modern conditions arose, the trend of legislation and judicial decision came more and more to adapt the recognized restrictions to new manifestations of conduct or

of dealing which it was thought justified the inference of intent to do the wrong which it had been the purpose to prevent from the beginning. The evolution is clearly pointed out in *National Cotton Oil Co.* v. *Texas*, 197 U. S. 115, 49 L. ed. 689, 25 Sup. Ct. Rep. 379, and *Shawnee Compress Co.* v. *Anderson*, 209 U. S. 423, 52 L. ed. 865, 28 Sup. Ct. Rep. 572; and, indeed, will be found to be illustrated in various aspects by the decisions of this court which have been concerned with the enforcement of the act we are now considering.

Without going into detail, and but very briefly surveying the whole field, it may be with accuracy said that the dread of enhancement of prices and of other wrongs which it was thought would flow from the undue limitation on competitive conditions caused by contracts or other acts of individuals or corporations led, as a matter of public policy, to the prohibition or treating as illegal all contracts or acts which were unreasonably restrictive of competitive conditions, either from the nature or character of the contract or act, or where the surrounding circumstances were such as to justify the conclusion that they had not been entered into or performed with the legitimate purpose of reasonably forwarding personal interest and developing trade, but, on the contrary, were of such a character as to give rise to the inference or presumption that they had been entered into or done with the intent to do wrong to the general public and to limit the right of individuals, thus restraining the free flow of commerce and tending to bring about the evils, such as enhancement of prices, which were considered to be against public policy. It is equally true to say that the survey of the legislation in this country on this subject from the beginning will show, depending, as it did, upon the economic conceptions which obtained at the time when the legislation was adopted or judicial decision was rendered, that contracts or acts were at one time deemed to be of such a character as to justify the inference of wrongful intent which were at another period thought not to be of that character. But this again, as we have seen, simply followed the line of development of the law of England.

Let us consider the language of the 1st and 2d sections, guided by the principle that where words are employed in a

statute which had at the time a well-known meaning at common law or in the law of this country, they are presumed to have been used in that sense unless the context compels to the contrary.

As to the 1st section, the words to be interpreted are: "Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce . . . is hereby declared to be illegal." As there is no room for dispute that the statute was intended to formulate a rule for the regulation of interstate and foreign commerce, the question is, What was the rule which it adopted?

In view of the common law and the law in this country as to restraint of trade, which we have reviewed, and the illuminating effect which that history must have under the rule to which we have referred, we think it results:

a. That the context manifests that the statute was drawn in the light of the existing practical conception of the law of restraint of trade, because it groups as within that class, not only contracts which were in restraint of trade in the subjective sense, but all contracts or acts which theoretically were attempts to monopolize, yet which in practice had come to be considered as in restraint of trade in a broad sense.

b. That in view of the many new forms of contracts and combinations which were being evolved from existing economic conditions, it was deemed essential by an all-embracing enumeration to make sure that no form of contract or combination by which an undue restraint of interstate or foreign commerce was brought about could save such restraint from condemnation. The statute under this view evidenced the intent not to restrain the right to make and enforce contracts, whether resulting from combinations or otherwise, which did not unduly restrain interstate or foreign commerce, but to protect that commerce from being restrained by methods, whether old or new, which would constitute an interference, — that is, an undue restraint.

c. And as the contracts or acts embraced in the provision were not expressly defined, since the enumeration addressed itself simply to classes of acts, those classes being broad enough to embrace every conceivable contract or combination which

could be made concerning trade or commerce or the subjects of such commerce, and thus caused any act done by any of the enumerated methods anywhere in the whole field of human activity to be illegal if in restraint of trade, it inevitably follows that the provision necessarily called for the exercise of judgment which required that some standard should be resorted to for the purpose of determining whether the prohibition contained in the statute had or had not in any given case been violated. Thus not specifying, but indubitably contemplating and requiring a standard, it follows that it was intended that the standard of reason which had been applied at the common law and in this country in dealing with subjects of the character embraced by the statute was intended to be the measure used for the purpose of determining whether, in a given case, a particular act had or had not brought about the wrong against which the statute provided.

And a consideration of the text of the 2d section serves to establish that it was intended to supplement the 1st, and to make sure that by no possible guise could the public policy embodied in the 1st section be frustrated or evaded. The prohibitions of the 2d embrace "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 . . ." By reference to the terms of § 8, it is certain that the word "person" clearly implies a corporation as well as an individual.

The commerce referred to by the words "in part," construed in the light of the manifest purpose of the statute, has both a geographical and a distributive significance; that is, it includes any portion of the United States and any one of the classes of things forming a part of interstate or foreign commerce.

Undoubtedly, the words "to monopolize" and "monopolize," as used in the section, reach every act bringing about the prohibited results. The ambiguity, if any, is involved in determining what is intended by monopolize. But this ambiguity is readily dispelled in the light of the previous history of the law of restraint of trade to which we have referred and the indication which it gives of the practical evolution by which monopoly

and the acts which produce the same result as monopoly, that is, an undue restraint of the course of trade, all came to be spoken of as, and to be indeed synonymous with, restraint of trade. In other words, having by the 1st section forbidden all means of monopolizing trade, that is, unduly restraining it by means of every contract, combination, etc., the 2d section seeks, if possible, to make the prohibitions of the act all the more complete and perfect by embracing all attempts to reach the end prohibited by the 1st section, that is, restraints of trade, by any attempt to monopolize, or monopolization thereof, even although the acts by which such results are attempted to be brought about or are brought about be not embraced within the general enumeration of the 1st section. And, of course, when the 2d section is thus harmonized with and made, as it was intended to be, the complement of the 1st, it becomes obvious that the criteria to be resorted to in any given case for the purpose of ascertaining whether violations of the section have been committed is the rule of reason guided by the established law and by the plain duty to enforce the prohibitions of the act, and thus the public policy which its restrictions were obviously enacted to subserve. And it is worthy of observation, as we have previously remarked concerning the common law, that although the statute, by the comprehensiveness of the enumerations embodied in both the 1st and 2d sections, makes it certain that its purpose was to prevent undue restraints of every kind or nature, nevertheless by the omission of any direct prohibition against monopoly in the concrete, it indicates a consciousness that the freedom of the individual right to contract, when not unduly or improperly exercised, was the most efficient means for the prevention of monopoly, since the operation of the centrifugal and centripetal forces resulting from the right to freely contract was the means by which monopoly would be inevitably prevented if no extraneous or sovereign power imposed it and no right to make unlawful contracts having a monopolistic tendency were permitted. In other words, that freedom to contract was the essence of freedom from undue restraint on the right to contract.

Clear as it seems to us is the meaning of the provisions of the statute in the light of the review which we have made, never-

theless, before definitively applying that meaning, it behooves us to consider the contentions urged on one side or the other concerning the meaning of the statute, which, if maintained, would give to it, in some aspects, a much wider and in every view, at least, a somewhat different, significance. And to do this brings us to the second question, which, at the outset, we have stated it was our purpose to consider and dispose of.

Second. The contentions of the parties as to the meaning of the statute, and the decisions of this court relied upon concerning those contentions.

In substance, the propositions urged by the government are reducible to this: That the language of the statute embraces every contract, combination, etc., in restraint of trade, and hence its text leaves no room for the exercise of judgment, but simply imposes the plain duty of applying its prohibitions to every case within its literal language. The error involved lies in assuming the matter to be decided. This is true, because, as the acts which may come under the classes stated in the 1st section and the restraint of trade to which that section applies are not specifically enumerated or defined, it is obvious that judgment must in every case be called into play in order to determine whether a particular act is embraced within the statutory classes, and whether, if the act is within such classes, its nature or effect causes it to be a restraint of trade within the intendment of the act. To hold to the contrary would require the conclusion either that every contract, act, or combination of any kind or nature, whether it operated a restraint on trade or not, was within the statute, and thus the statute would be destructive of all right to contract or agree or combine in any respect whatever as to subjects embraced in interstate trade or commerce, or, if this conclusion were not reached, then the contention would require it to be held that, as the statute did not define the things to which it related, and excluded resort to the only means by which the acts to which it relates could be ascertained, — the light of reason, — the enforcement of the statute was impossible because of its uncertainty. The merely generic enumeration which the statute makes of the acts to which it refers, and the absence of any definition of restraint of trade as

used in the statute, leaves room for but one conclusion, which is, that it was expressly designed not to unduly limit the application of the act by precise definition, but, while clearly fixing a standard, that is, by defining the ulterior boundaries which could not be transgressed with impunity, to leave it to be determined by the light of reason, guided by the principles of law and the duty to apply and enforce the public policy embodied in the statute, in every given case whether any particular act or contract was within the contemplation of the statute.

But, it is said, persuasive as these views may be, they may not be here applied, because the previous decisions of this court have given to the statute a meaning which expressly excludes the construction which must result from the reasoning stated. The cases are *United States* v. *Trans-Missouri Freight Asso.* and *United States* v. *Joint Traffic Asso.* Both the cases involved the legality of combinations or associations of railroads engaged in interstate commerce for the purpose of controlling the conduct of the parties to the association or combination in many particulars. The association or combination was assailed in each case as being in violation of the statute. It was held that they were. It is undoubted that, in the opinion in each case, general language was made use of, which, when separated from its context, would justify the conclusion that it was decided that reason could not be resorted to for the purpose of determining whether the acts complained of were within the statute. It is, however, also true that the nature and character of the contract or agreement in each case was fully referred to, and suggestions as to their unreasonableness pointed out in order to indicate that they were within the prohibitions of the statute. As the cases cannot, by any possible conception, be treated as authoritative without the certitude that reason was resorted to for the purpose of deciding them, it follows as a matter of course that it must have been held by the light of reason, since the conclusion could not have been otherwise reached, that the assailed contracts or agreements were within the general enumeration of the statute, and that their operation and effect brought about the restraint of trade which the statute prohibited. This being inevitable, the deduction can in reason only be this: That in the

cases relied upon, it having been found that the acts complained of were within the statute, and operated to produce the injuries which the statute forbade, that resort to reason was not permissible in order to allow that to be done which the statute prohibited. This being true, the rulings in the case relied upon, when rightly appreciated, were therefore this, and nothing more: That as considering the contracts and agreements, their necessary effect, and the character of the parties by whom they were made, they were clearly restraints of trade within the purview of the statute, they could not be taken out of that category by indulging in general reasoning as to the expediency or non-expediency of having made the contracts, or the wisdom or want of wisdom of the statute which prohibited their being made. That is to say, the cases but decided that the nature and character of the contracts, creating, as they did, a conclusive presumption which brought them within the statute, such result was not to be disregarded by the substitution of a judicial appreciation of what the law ought to be for the plain judicial duty of enforcing the law as it was made.

But aside from reasoning, it is true to say that the cases relied upon do not, when rightly construed, sustain the doctrine contended for, is established by all of the numerous decisions of this court which have applied and enforced the anti-trust act, since they all, in the very nature of things, rest upon the premise that reason was the guide by which the provisions of the act were in every case interpreted. Indeed, intermediate the decision of the two cases, that is, after the decision in the Freight Association Case, and before the decision in the Joint Traffic Case, the case of *Hopkins* v. *United States*, was decided, the opinion being delivered by Mr. Justice Peckham, who wrote both the opinions in the Freight Association and in the Joint Traffic Cases. And, referring in the Hopkins Case to the broad claim made as to the rule of interpretation announced in the Freight Association Case, it was said (page 592):

To treat as condemned by the act all agreements under which, as a result, the cost of conducting an interstate commercial business may be increased, would enlarge the application of the act far beyond

the fair meaning of the language used. There must be some direct and immediate effect upon interstate commerce in order to come within the act.

And in the Joint Traffic case this statement was expressly reiterated and approved and illustrated by example. Like limitation on the general language used in Freight Association and Joint Traffic cases is also the clear result of *E. Bement & Sons* v. *National Harrow Co.*, etc., etc.

If the criterion by which it is to be determined in all cases whether every contract, combination, etc., is a restraint of trade within the intendment of the law, is the direct or indirect effect of the acts involved, then of course the rule of reason becomes the guide, and the construction which we have given the statute, instead of being refuted by the cases relied upon, is by those cases demonstrated to be correct. This is true, because the construction which we have deduced from the history of the act and the analysis of its text is simply that in every case where it is claimed that an act or acts are in violation of the statute, the rule of reason, in the light of the principles of law and the public policy which the act embodies, must be applied. From this it follows, since that rule and the result of the test as to direct or indirect, in their ultimate aspect, come to one and the same thing, that the difference between the two is therefore only that which obtains between things which do not differ at all.

If it be true that there is this identity of result between the rule intended to be applied in the Freight Association case, that is, the rule of direct and indirect, and the rule of reason which, under the statute as we construe it, should be here applied, it may be asked how was it that, in the opinion in the Freight Association case, much consideration was given to the subject of whether the agreement or combination which was involved in that case could be taken out of the prohibitions of the statute upon the theory of its reasonableness. The question is pertinent and must be fully and frankly met; for if it be now deemed that the Freight Association case was mistakenly decided or too broadly stated, the doctrine which it announced should be either expressly overruled or limited.

The confusion which gives rise to the question results from failing to distinguish between the want of power to take a case which, by its terms or the circumstances which surrounded it, considering among such circumstances the character of the parties, is plainly within the statute, out of the operation of the statute by resort to reason in effect to establish that the contract ought not to be treated as within the statute, and the duty in every case where it becomes necessary from the nature and character of the parties to decide whether it was within the statute, to pass upon that question by the light of reason. This distinction, we think, serves to point out what, in its ultimate conception, was the thought underlying the reference to the rule of reason made in the Freight Association case,— especially when such reference is interpreted by the context of the opinion and in the light of the subsequent opinion in the Hopkins case and in *Cincinnati, P. B. S. & P. Packet Co.* v. *Bay.*

And in order not in the slightest degree to be wanting in frankness, we say that in so far, however, as by separating the general language used in the opinions in the Freight Association and Joint Traffic cases from the context and the subject and parties with which the cases were concerned, it may be conceived that the language referred to conflicts with the construction which we give the statute, they are necessarily now limited and qualified. We see no possible escape from this conclusion if we are to adhere to the many cases decided in this court in which the anti-trust law has been applied and enforced, and if the duty to apply and enforce that law in the future is to continue to exist. The first is true, because the construction which we now give the statute does not in the slightest degree conflict with a single previous case decided concerning the anti-trust law, aside from the contention as to the Freight Association and Joint Traffic cases, and because every one of those cases applied the rule of reason for the purpose of determining whether the subject before the court was within the statute. The second is also true, since, as we have already pointed out, unaided by the light of reason it is impossible to understand how the statute may in the future be enforced and the public policy which it establishes be made efficacious.

So far as the objections of the appellants are concerned, they are all embraced under two headings:

a. That the act, even if the averments of the bill be true, cannot be constitutionally applied, because to do so would extend the power of Congress to subjects *dehors* the reach of its authority to regulate commerce, by enabling that body to deal with mere questions of production of commodities within the states. But all the structure upon which this argument proceeds is based upon the decision in *United States* v. *E. C. Knight Co.*[1] The view, however, which the argument takes of that case, and the arguments based upon that view, have been so repeatedly pressed upon this court in connection with the interpretation and enforcement of the anti-trust act, and have been so necessarily and expressly decided to be unsound, as to cause the contentions to be plainly foreclosed and to require no express notice.

b. Many arguments are pressed in various forms of statement which in substance amount to contending that the statute cannot be applied under the facts of this case without impairing rights of property and destroying the freedom of contract or trade which is essentially necessary to the well-being of society, and which, it is insisted, is protected by the constitutional guaranty of due process of law. But the ultimate foundation of all these arguments is the assumption that reason may not be resorted to in interpreting and applying the statute, and therefore that the statute unreasonably restricts the right to contract, and unreasonably operates upon the right to acquire and hold property. As the premise is demonstrated to be unsound by the construction we have given the statute, of course the propositions which rest upon that premise need not be further noticed.

So far as the arguments proceed upon the conception that, in view of the generality of the statute, it is not susceptible of being enforced by the courts because it cannot be carried out without a judicial exertion of legislative power, they are clearly unsound. The statute certainly generically enumerates the character of acts which it prohibits and the wrong which it was intended to prevent. The propositions therefore insist that, consistently with the fundamental principles of due process of law, it never can be

[1] P. 506, *supra*.

left to the judiciary to decide whether, in a given case, particular acts come within a generic statutory provision. But to reduce the propositions, however, to this, their final meaning, makes it clear that in substance they deny the existence of essential legislative authority, and challenge the right of the judiciary to perform duties which that department of the government has exerted from the beginning. This is so clear as to require no elaboration. Yet, let us demonstrate that which needs no demonstration, by a few obvious examples. Take, for instance, the familiar cases where the judiciary is called upon to determine whether a particular act or acts are within a given prohibition, depending upon wrongful intent. Take questions of fraud. Consider the power which must be exercised in every case where the courts are called upon to determine whether particular acts are invalid which are, abstractly speaking, in and of themselves valid, but which are asserted to be invalid because of their direct effect upon interstate commerce.

We come, then, to the third proposition requiring consideration, viz:

Third. The facts and the application of the statute to them.

Beyond dispute the proofs establish substantially as alleged in the bill the following facts:

1. The creation of the Standard Oil Company of Ohio.

2. The organization of the Standard Oil Trust of 1882, and also a previous one of 1879, not referred to in the bill, and the proceedings in the supreme court of Ohio, culminating in a decree based upon the finding that the company was unlawfully a party to that trust; the transfer by the trustees of stocks in certain of the companies; the contempt proceedings; and, finally, the increase of the capital of the Standard Oil Company of New Jersey and the acquisition by that company of the shares of the stock of the other corporations in exchange for its certificates.

The vast amount of property and the possibilities of far-reaching control which resulted from the facts last stated are shown by the statement which we have previously annexed concerning the parties to the trust agreement of 1882, and the corporations whose stock was held by the trustees under the trust, and which came therefore to be held by the New Jersey corpora-

tion. But these statements do not with accuracy convey an appreciation of the situation as it existed at the time of the entry of the decree below, since, during the more than ten years which elapsed between the acquiring by the New Jersey corporation of the stock and other property which was formerly held by the trustees under the trust agreement, the situation, of course, had somewhat changed, — a change which, when analyzed in the light of the proof, we think establishes that the result of enlarging the capital stock of the New Jersey company and giving it the vast power to which we have referred produced its normal consequence; that is, it gave to the corporation, despite enormous dividends and despite the dropping out of certain corporations enumerated in the decree of the court below, an enlarged and more perfect sway and control over the trade and commerce in petroleum and its products.

Giving to the facts just stated the weight which it was deemed they were entitled to, in the light afforded by the proof of other cognate facts and circumstances, the court below held that the acts and dealings established by the proof operated to destroy the "potentiality of competition" which otherwise would have existed to such an extent as to cause the transfers of stock which were made to the New Jersey corporation and the control which resulted over the many and various subsidiary corporations to be a combination or conspiracy in restraint of trade, in violation of the 1st section of the act, but also to be an attempt to monopolize and monopolization bringing about a perennial violation of the 2d section.

We see no cause to doubt the correctness of these conclusions, considering the subject from every aspect; that is, both in view of the facts established by the record and the necessary operation and effect of the law as we have construed it upon the inferences deducible from the facts, for the following reasons:

a. Because the unification of power and control over petroleum and its products which was the inevitable result of the combining in the New Jersey corporation by the increase of its stock and the transfer to it of the stocks of so many other corporations, aggregating so vast a capital, gives rise, in and of itself, in the absence of countervailing circumstances, to say the least, to the

prima facie presumption of intent and purpose to maintain the dominancy over the oil industry, not as a result of normal methods of industrial development, but by new means of combination which were resorted to in order that greater power might be added than would otherwise have arisen had normal methods been followed, the whole with the purpose of excluding others from the trade, and thus centralizing in the combination a perpetual control of the movements of petroleum and its products in the channels of interstate commerce.

b. Because the prima facie presumption of intent to restrain trade, to monopolize and to bring about monopolization, resulting from the act of expanding the stock of the New Jersey corporation and vesting it with such vast control of the oil industry, is made conclusive by considering (1) the conduct of the persons or corporations who were mainly instrumental in bringing about the extension of power in the New Jersey corporation before the consummation of that result and prior to the formation of the trust agreements of 1879 and 1882; (2) by considering the proof as to what was done under those agreements and the acts which immediately preceded the vesting of power in the New Jersey corporation, as well as by weighing the modes in which the power vested in that corporation has been exerted and the results which have arisen from it.

Recurring to the acts done by the individuals or corporations who were mainly instrumental in bringing about the expansion of the New Jersey corporation during the period prior to the formation of the trust agreements of 1879 and 1882, including those agreements, not for the purpose of weighing the substantial merit of the numerous charges of wrongdoing made during such period, but solely as an aid for discovering intent and purpose, we think no disinterested mind can survey the period in question without being irresistibly driven to the conclusion that the very genius for commercial development and organization which it would seem was manifested from the beginning soon begot an intent and purpose to exclude others which was frequently manifested by acts and dealings wholly inconsistent with the theory that they were made with the single conception of advancing the development of business power by usual meth-

ods, but which, on the contrary, necessarily involved the intent to drive others from the field and to exclude them from their right to trade, and thus accomplish the mastery which was the end in view. And, considering the period from the date of the trust agreements of 1879 and 1882, up to the time of the expansion of the New Jersey corporation, the gradual extension of the power over the commerce in oil which ensued, the decision of the supreme court of Ohio, the tardiness or reluctance in conforming to the commands of that decision, the methods first adopted and that which finally culminated in the plan of the New Jersey corporation, all additionally serve to make manifest the continued existence of the intent which we have previously indicated, and which, among other things, impelled the expansion of the New Jersey corporation. The exercise of the power which resulted from that organization fortifies the foregoing conclusions, since the development which came, the acquisition here and there which ensued of every efficient means by which competition could have been asserted, the slow but resistless methods which followed by which means of transportation were absorbed and brought under control, the system of marketing which was adopted by which the country was divided into districts and the trade in each district in oil was turned over to a designated corporation within the combination, and all others were excluded, all lead the mind up to a conviction of a purpose and intent which we think is so certain as practically to cause the subject not to be within the domain of reasonable contention.

The inference that no attempt to monopolize could have been intended, and that no monopolization resulted from the acts complained of, since it is established that a very small percentage of the crude oil produced was controlled by the combination, is unwarranted. As substantial power over the crude product was the inevitable result of the absolute control which existed over the refined product, the monopolization of the one carried with it the power to control the other; and if the inferences which this situation suggests were developed, which we deem it unnecessary to do, they might well serve to add additional cogency to the presumption of intent to monopolize which we have found arises from the unquestioned proof on other subjects.

We are thus brought to the last subject which we are called upon to consider, viz.:

Fourth. The remedy to be administered.

Let us, then, as a means of accurately determining what relief we are to afford, first come to consider what relief was afforded by the court below, in order to fix how far it is necessary to take from or add to that relief, to the end that the prohibitions of the statute may have complete and operative force.

The court below, by virtue of §§ 1, 2, and 4 of its decree, which we have in part excerpted in the margin, [Omitted.] adjudged that the New Jersey corporation, in so far as it held the stock of the various corporations recited in §§ 2 and 4 of the decree, or controlled the same, was a combination in violation of the 1st section of the act, and an attempt to monopolize or a monopolization contrary to the 2d section of the act. It commanded the dissolution of the combination, and therefore in effect directed the transfer by the New Jersey corporation back to the stockholders of the various subsidiary corporations entitled to the same of the stock which had been turned over to the New Jersey company in exchange for its stock. To make this command effective, § 5 of the decree forbade the New Jersey corporation from in any form or manner exercising any ownership or exerting any power directly or indirectly in virtue of its apparent title to the stocks of the subsidiary corporations, and prohibited those subsidiary corporations from paying any dividends to the New Jersey corporations, or doing any act which would recognize further power in that company, except to the extent that it was necessary to enable that company to transfer the stock. So far as the owners of the stock of the subsidiary corporations and the corporations themselves were concerned after the stock had been transferred, § 6 of the decree enjoined them from in any way conspiring or combining to violate the act, or to monopolize or attempt to monopolize in virtue of their ownership of the stock transferred to them, and prohibited all agreements between the subsidiary corporations or other stockholders in the future, tending to produce or bring about further violations of the act.

By § 7, pending the accomplishment of the dissolution of the

combination by the transfer of stock, and until it was consummated, the defendants named in § 1, constituting all the corporations to which we have referred, were enjoined from engaging in or carrying on interstate commerce. And by § 9, among other things, a delay of thirty days was granted for the carrying into effect of the directions of the decree.

So far as the decree held that the ownership of the stock of the New Jersey corporation constituted a combination in violation of the 1st section and an attempt to create a monopoly or to monopolize under the 2d section, and commanded the dissolution of the combination, the decree was clearly appropriate. And this also is true of § 5 of the decree, which restrained both the New Jersey corporation and the subsidiary corporations from doing anything which would recognize or give effect to further ownership in the New Jersey corporation of the stocks which were ordered to be retransferred.

Our conclusion is that the decree below was right and should be affirmed, except as to the minor matters concerning which we have indicated the decree should be modified.

And it is so ordered.

Mr. Justice Harlan, concurring in part and dissenting in part:

A sense of duty constrains me to express the objections which I have to certain declarations in the opinion just delivered on behalf of the court.

I concur in holding that the Standard Oil Company of New Jersey and its subsidiary companies constitute a combination in restraint of interstate commerce, and that they have attempted to monopolize and have monopolized parts of such commerce, — all in violation of what is known as the anti-trust act of 1890. The evidence in this case overwhelmingly sustained that view and led the circuit court, by its final decree, to order the dissolution of the New Jersey corporation and the discontinuance of the illegal combination between that corporation and its subsidiary companies.

In my judgment, the decree below should have been affirmed without qualification. But the court, while affirming the decree, directs some modifications in respect of what it characterizes as "minor matters." It is to be apprehended that those modifica-

tions may prove to be mischievous. In saying this, I have particularly in view the statement in the opinion that "it does not necessarily follow because an illegal restraint of trade or an attempt to monopolize or a monopolization resulted from the combinations and the transfer of the stocks of the subsidiary corporation to the New Jersey corporation, that a like restraint of trade or attempt to monopolize or monopolization would necessarily arise from agreements between one or more of the subsidiary corporations after the transfer of the stock by the New Jersey corporation." Taking this language, in connection with other parts of the opinion, the subsidiary companies are thus, in effect, informed — unwisely, I think — that although the New Jersey corporation, being an illegal combination, must go out of existence, *they* may join in an agreement *to restrain commerce* among the states if such restraint be not "undue."

In order that my objections to certain parts of the court's opinion may distinctly appear, I must state the circumstances under which Congress passed the anti-trust act, and trace the course of judicial decisions as to its meaning and scope. This is the more necessary because the court by its decision, when interpreted by the language of its opinion, has not only upset the long-settled interpretation of the act, but has usurped the constitutional functions of the legislative branch of the government. With all due respect for the opinions of others, I feel bound to say that what the court has said may well cause some alarm for the integrity of our institutions. Let us see how the matter stands.

All who recall the condition of the country in 1890 will remember that there was everywhere, among the people generally, a deep feeling of unrest. The nation had been rid of human slavery, — fortunately, as all now feel, — but the conviction was universal that the country was in real danger from another kind of slavery sought to be fastened on the American people; namely, the slavery that would result from aggregations of capital in the hands of a few individuals and corporations controlling, for their own profit and advantage exclusively, the entire business of the country, including the production and sale of the necessaries of life. Such a danger was thought to be

then imminent, and all felt that it must be met firmly and by such statutory regulations as would adequately protect the people against oppression and wrong. Congress therefore took up the matter and gave the whole subject the fullest consideration. All agreed that the national government could not, by legislation, regulate the domestic trade carried on wholly within the several states; for power to regulate such trade remained with, because never surrended by, the states. But, under authority expressly granted to it by the Constitution, Congress could regulate commerce among the several states and with foreign states. Its authority to regulate such commerce was and is paramount, due force being given to other provisions of the fundamental law, devised by the fathers for the safety of the government and for the protection and security of the essential rights inhering in life, liberty, and property.

Guided by these considerations, and to the end that the people, *so far as interstate commerce* was concerned, might not be dominated by vast combinations and monopolies, having power to advance their own selfish ends, regardless of the general interests and welfare, Congress passed the anti-trust act of 1890 in these words. [P. 484, *supra*.]

I have made these extended extracts from the opinion of the court in the Trans-Missouri Freight case in order to show beyond question that the point was there urged by counsel that the anti-trust act condemned *only* contracts, combinations, trusts, and conspiracies that were in *unreasonable* restraint of interstate commerce, and that the court in clear and decisive language met that point. It adjudged that Congress had in unequivocal words declared that "*every* contract, combination in the form of trust or otherwise, or conspiracy, in restraint of commerce among the several states," shall be illegal, and that no distinction, *so far as interstate commerce was concerned*, was to be tolerated between restraints of such commerce as were undue or unreasonable, and restraints that were due or reasonable. With full knowledge of the then condition of the country and of its business, Congress determined to meet, and did meet, the situation by an absolute, statutory prohibition of "*every* contract, combination in the form of trusts or otherwise, in restraint of

trade or commerce." Still more; in response to the suggestion by able counsel that Congress intended only to strike down such contracts, combinations, and monopolies as unreasonably restrained interstate commerce, this court, in words too clear to be misunderstood, said that to so hold was "to read into the act by way of *judicial legislation*, an exception not placed there by the lawmaking branch of the government." "This," the court said, as we have seen, "*we cannot* and *ought not* to do."

It thus appears that fifteen years ago, when the purpose of Congress in passing the anti-trust act was fresh in the minds of courts, lawyers, statesmen, and the general public, this court expressly declined to indulge in judicial legislation, by inserting in the act the word "unreasonable" or any other word of like import. It may be stated here that the country at large accepted this view of the act, and the Federal courts throughout the entire country enforced its provisions according to the interpretation given in the Freight Association case. What, then, was to be done by those who questioned the soundness of the interpretation placed on the act by this court in that case? As the court had decided that to insert the word "unreasonable" in the act would be "judicial legislation" on its part, the only alternative left to those who opposed the decision in that case was to induce Congress to so *amend* the act as to recognize the right to restrain interstate commerce to a *reasonable* extent. The public press, magazines, and law journals, the debates in Congress, speeches, and addresses by public men and jurists, all contain abundant evidence of the general understanding that the meaning, extent, and scope of the anti-trust act had been judicially determined by this court, and that the only question remaining open for discussion was the wisdom of the policy declared by the act, — a matter that was exclusively within the cognizance of Congress. But at every session of Congress since the decision of 1896, the lawmaking branch of the government, with full knowledge of that decision, has refused to change the policy it had declared, or to so amend the act of 1890, as to except from its operation contracts, combinations, and trusts that *reasonably* restrain interstate commerce.

But those who were in combinations that were illegal did not

despair. They at once set up the baseless claim that the decision of 1896 disturbed the "business interests of the country," and let it be known that they would never be content until the rule was established that would permit interstate commerce to be subjected to *reasonable* restraints. Finally, an opportunity came again to raise the same question which this court had, upon full consideration, determined in 1896. I now allude to the case of *United States* v. *Joint Traffic Asso.*

These utterances, taken in connection with what was previously said in the Trans-Missouri Freight case, show so clearly and affirmatively as to admit of no doubt that this court, many years ago, upon the fullest consideration, interpreted the anti-trust act as prohibiting and making illegal not only *every* contract or combination, in whatever form, which was in restraint of interstate commerce, without regard to its reasonableness or unreasonableness, but all monopolies or attempt to monopolize "any part" of such trade or commerce. Let me refer to a few other cases in which the scope of the decision in the Freight Association case was referred to.

After what has been adjudged, upon full consideration, as to the meaning and scope of the anti-trust act, and in view of the usages of this court when attorneys for litigants have attempted to reopen questions that have been deliberately decided, I confess to no little surprise as to what has occurred in the present case. The court says that the previous cases, above cited, "cannot by any possible conception be treated as authoritative without the certitude that *reason* was resorted to for the purpose of deciding them." And its opinion is full of intimations that this court proceeded in those cases, so far as the present question is concerned, without being guided by the "rule of reason" or "the light of reason." It is more than once intimated, if not suggested, that if the anti-trust act is to be construed as prohibiting *every* contract or combination, of whatever nature, which is in fact in restraint of commerce, regardless of the reasonableness or unreasonableness of such restraint, that fact would show that the court had not proceeded, in its decision, according to "the light of reason," but had disregarded the "rule of reason." If the court, in those cases, was wrong in its construction of the

act, it is certain that it fully apprehended the views advanced by learned counsel in previous cases and pronounced them to be untenable. The published reports place this beyond all question. The opinion of the court was delivered by a justice of wide experience as a judicial officer, and the court had before it the Attorney-General of the United States and lawyers who were recognized, on all sides, as great leaders in their profession. The same eminent jurist who delivered the opinion in the Trans-Missouri case delivered the opinion in the Joint Traffic case, while the association in the latter case was represented by lawyers whose ability was universally recognized. Is it to be supposed that any point escaped notice in those cases when we think of the sagacity of the justice who expressed the views of the court, or of the ability of the profound, astute lawyers who sought such an interpretation of the act as would compel the court to insert words in the statute which Congress had not put there, and the insertion of which words would amount to "judicial legislation"? Now this court is asked to do that which it has distinctly declared it could not and would not do, and has now done what it then said it could not constitutionally do. It has, by mere interpretation, modified the act of Congress, and deprived it of practical value as a defensive measure against the evils to be remedied. On reading the opinion just delivered, the first inquiry will be, that as the court is unanimous in holding that the particular things done by the Standard Oil Company and its subsidiary companies, in this case, were illegal under the anti-trust act, whether those things were in reasonable or unreasonable restraint of interstate commerce, why was it necessary to make an elaborate argument, as is done in the opinion, to show that according to the "rule of reason" the act as passed by Congress should be interpreted as if it contained the word "unreasonable" or the word "undue"? The only answer which, in frankness, can be given to this question, is, that the court intends to decide that its deliberate judgment, fifteen years ago, to the effect that the act permitted no restraint whatever of interstate commerce, whether reasonable or unreasonable, was not in accordance with the "rule of reason." In effect the court says that it will now, for the first time, bring the discussion

under the "light of reason," and apply the "rule of reason" to the questions to be decided. I have the authority of this court for saying that such a course of proceeding on its part would be "judicial legislation."

Still more, what is now done involves a serious departure from the settled usages of this court. Counsel have not ordinarily been allowed to discuss questions already settled by previous decisions. When counsel in the present case insisted upon a reversal of the former rulings of this court, and asked such an interpretation of the anti-trust act, as would allow reasonable restraints of interstate commerce, this court, in deference to established practice, should, I submit, have said to them: "That question, according to our practice, is not open for further discussion here. This court long ago deliberately held (1) that the act, interpreting its words in their ordinary acceptation, prohibits *all* restraints of interstate commerce by combinations in whatever form, and whether reasonable or unreasonable; (2) the question relates to matters of public policy in reference to commerce among the states and with foreign nations, and Congress alone can deal with the subject; (3) this court would encroach upon the authority of Congress if, under the guise of construction, it should assume to determine a matter of public policy; (4) the parties must go to Congress and obtain an amendment of the anti-trust act if they think this court was wrong in its former decisions; and (5) this court cannot and will not *judicially legislate*, since its function is to declare the law, while it belongs to the legislative department to make the law." Such a course, I am sure, would not have offended the "rule of reason."

But my brethren, in their wisdom, have deemed it best to pursue a different course. They have now said to those who condemn our former decisions and who object to all legislative prohibitions of contracts, combinations, and trusts in restraint of interstate commerce, "You may *now* restrain such commerce, provided you are reasonable about it; only take care that the restraint is not undue." The disposition of the case under consideration, according to the views of the defendants, will, it is claimed, quiet and give rest to "the business of the country." On the contrary, I have a strong conviction that it will throw

the business of the country into confusion and invite widely-extended and harassing litigation, the injurious effects of which will be felt for many years to come. When Congress prohibited *every* contract, combination, or monopoly, in restraint of commerce, it prescribed a simple, definite rule that all could understand, and which could be easily applied by every one wishing to obey the law, and not to conduct their business in violation of law. But now, it is to be feared, we are to have, in cases without number, the constantly recurring inquiry — difficult to solve by proof — whether the particular contract, combination, or trust involved in each case is or is not an "unreasonable" or "undue" restraint of trade. Congress, in effect, said that there should be *no* restraint of trade *in any form*, and this court solemnly adjudged many years ago that Congress meant what it thus said in clear and explicit words, and that it *could not* add to the words of the act. But those who condemn the action of Congress are now, in effect, informed that the courts will allow such restraint of interstate commerce as are shown not to be unreasonable or undue.

It remains for me to refer, more fully than I have heretofore done, to another, and, in my judgment, — if we look to the future, — the most important, aspect of this case. That aspect concerns the usurpation by the judicial branch of the government of the functions of the legislative department. The illustrious men who laid the foundations of our institutions deemed no part of the national Constitution of more consequence or more essential to the permanency of our form of government than the provisions under which were distributed the powers of government among three separate, equal, and coördinate departments, — legislative, executive, and judicial. This was at that time a new feature of governmental regulation among the nations of the earth, and it is deemed by the people of every section of our own country as most vital in the workings of a representative republic whose Constitution was ordained and established in order to accomplish the objects stated in its Preamble by the means, *but only by the means*, provided, either expressly or by necessary implication, by the instrument itself. No department of that government can constitutionally exercise the powers committed strictly to another and separate department.

I said at the outset that the action of the court in this case might well alarm thoughtful men who revered the Constitution. I meant by this that many things are intimated and said in the court's opinion which will not be regarded otherwise than as sanctioning an invasion by the judiciary of the constitutional domain of Congress, — an attempt by interpretation to soften or modify what some regard as a harsh public policy. This court, let me repeat, solemnly adjudged many years ago that it could not, except by "*judical legislation,*" read words into the anti-trust act not put there by Congress, and which, being inserted, gives it a meaning which the words of the act, as passed, if properly interpreted, would not justify. The court has decided that it could not thus change a public policy formulated and declared by Congress; that Congress has paramount authority to regulate interstate commerce, and that it alone can change a policy once inaugurated by legislation. The courts have nothing to do with the wisdom or policy of an act of Congress. Their duty is to ascertain the will of Congress, and if the statute embodying the expression of that will is constitutional, the courts must respect it. They have no function to declare a public policy, nor to *amend legislative enactments.* "What is termed the policy of the government with reference to any particular legislation," as this court has said, "is generally a very uncertain thing, upon which all sorts of opinions, each variant from the other, may be formed by different persons. It is a ground much too unstable upon which to rest the judgment of the court in the interpretation of statutes." *Hadden* v. *The Collector* (*Hadden* v. *Banrey*), 5 Wall. 107, 18 L. ed. 518. Nevertheless, if I do not misapprehend its opinion, the court has now read into the act of Congress words which are not to be found there, and has thereby done that which it adjudged in 1896 and 1898 could not be done without violating the Constitution; namely, by interpretation of a statute changed a public policy declared by the legislative department.

After many years of public service at the national capital, and after a somewhat close observation of the conduct of public affairs, I am impelled to say that there is abroad in our land a most harmful tendency to bring about the amending of constitutions and legislative enactments by means alone of judicial con-

struction. As a public policy has been declared by the legislative department in respect of interstate commerce, over which Congress has entire control, under the Constitution, all concerned must patiently submit to what has been lawfully done, until the people of the United States — the source of all national power — shall, in their own time, upon reflection and through the legislative department of the government, require a change of that policy. There are some who say that it is a part of one's liberty to conduct commerce among the states without being subject to governmental authority. But that would not be liberty regulated by law, and liberty which cannot be regulated by law is not to be desired. The supreme law of the land, which is binding alike upon all, — upon Presidents, Congresses, the courts and the people, — gives to Congress, and to Congress alone, authority to regulate interstate commerce, and when Congress forbids *any* restraint of such commerce, in any form, all must obey its mandate. To overreach the action of Congress merely by judicial construction, that is, by indirection, is a blow at the integrity of our governmental system, and in the end will prove most dangerous to all. Mr. Justice Bradley wisely said, when on this bench, that illegitimate and unconstitutional practices get their first footing by silent approaches and slight deviations from legal modes of legal procedure. We shall do well to heed the warnings of that great jurist.

I do not stop to discuss the merits of the policy embodied in the anti-trust act of 1890; for, as has been often adjudged, the courts, under our constitutional system, have no rightful concern with the wisdom or policy of legislation enacted by that branch of the government which alone can make laws.

For the reasons stated, while concurring in the general affirmance of the decree of the Circuit Court, I dissent from that part of the judgment of this court which directs the modification of the decree of the Circuit Court, as well as from those parts of the opinion which, in effect, assert authority in this court to insert words in the anti-trust act which Congress did not put there, and which, being inserted, Congress is made to declare, as part of the public policy of the country, what it has not chosen to declare.

THE TOBACCO COMPANY CASE[1]

Mr. Chief Justice White delivered the opinion of the court:

We shall divide our investigation of the case into three subjects: First, the undisputed facts; second, the meaning of the anti-trust law, and its application, as correctly construed, to the ultimate conclusions of fact deducible from the proof; third, the remedies to be applied.

First. Undisputed facts. [Practically a repetition of Chapter VIII, *supra.*]

The construction and application of the anti-trust act.

If the anti-trust law is applicable to the entire situation here presented, and is adequate to afford complete relief for the evils which the United States insists that situation presents, it can only be because that law will be given a more comprehensive application than has been affixed to it in any previous decision. This will be the case because the undisputed facts as we have stated them involve questions as to the operation of the anti-trust law not hitherto presented in any case. Thus, even if the ownership of stock by the American Tobacco Company in the accessory and subsidiary companies, and the ownership of stock in any of those companies among themselves, were held, as was decided in the Standard Oil Company case, to be a violation of the act, and all relations resulting from such stock ownership were therefore set aside, the question would yet remain whether the principal defendant, the American Tobacco Company, and the five accessory defendants, even when devested of their stock ownership in other corporations, by virtue of the power which they would continue to possess, even although thus stripped, would amount to a violation of both the 1st and 2d sections of the act. Again, if it were held that the corporation, the existence whereof was due to a combination between such companies and other companies, was a violation of the act, the question would remain whether such of the companies as did not owe their existence and power to combinations, but whose power alone arose from

[1] *U. S.* v. *American Tobacco Co. etc.;* 31 Supreme Court Rep. 632; 221 U. S. Rep. 181; decided May 29, 1911. Many citations are omitted without indication and the opinion is greatly abridged. The economic facts are given in Chapter VIII, *supra.*

the exercise of the right to acquire and own property, would be amenable to the prohibitions of the act. Yet further: Even if this proposition was held in the affirmative, the question would remain whether the principal defendant, the American Tobacco Company, when stripped of its stock ownership, would be, in and of itself, within the prohibitions of the act, although that company was organized and took being before the anti-trust act was passed. Still further, the question would yet remain whether particular corporations which, when bereft of the power which they possessed as resulting from stock ownership, although they were not inherently possessed of a sufficient residuum of power to cause them to be, in and of themselves, either a restraint of trade or a monopolization or an attempt to monopolize, should nevertheless be restrained because of their intimate connection and association with other corporations found to be within the prohibitions of the act. The necessity of relief as to all these aspects, we think, seemed to the government so essential, and the difficulty of giving to the act such a comprehensive and coherent construction as would be adequate to enable it to meet the entire situation, led to what appears to us to be in their essence a resort to methods of construction not compatible one with the other. And the same apparent conflict is presented by the views of the act taken by the defendants when their contentions are accurately tested. Thus, the government, for the purpose of fixing the illegal character of the original combinations which organized the old American Tobacco Company, asserts that the illegal character of the combination is plainly shown because the combination was brought about to stay the progress of a flagrant and ruinous trade war. In other words, the contention is that, as the act forbids every contract and combination, it hence prohibits a reasonable and just agreement made for the purpose of ending a trade war. But, as thus construing the act by the rule of the letter which kills would necessarily operate to take out of the reach of the act some of the accessory and many subsidiary corporations, the existence of which depends not at all upon combination or agreement or contract, but upon mere purchasers of property, it is insisted in many forms of argument that the rule of construction to be applied must be the spirit and

intent of the act, and therefore its prohibitions must be held to extend to acts even if not within the literal terms of the statute, if they are within its spirit, because done with an intent to bring about the harmful results which it was the purpose of the statute to prohibit. So as to the defendants. While it is argued on the one hand that the forms by which various properties were acquired, in view of the letter of the act, exclude many of the assailed transactions from condemnation, it is yet urged that, giving to the act the broad construction which it should rightfully receive, whatever may be the form, no condemnation should follow, because, looking at the case as a whole, every act assailed is shown to have been but a legitimate and lawful result of the exertion of honest business methods, brought into play for the purpose of advancing trade, instead of with the object of obstructing and restraining the same. But the difficulties which arise from the complexity of the particular dealings which are here involved and the situation which they produce, we think grows out of a plain misconception of both the letter and spirit of the anti-trust act. We say of the letter, because, while seeking by a narrow rule of the letter to include things which it is deemed would otherwise be excluded, the contention really destroys the great purpose of the act, since it renders it impossible to apply the law to a multitude of wrongful acts which would come within the scope of its remedial purposes by resort to a reasonable construction, although they would not be within its reach by a too narrow and unreasonable adherence to the strict letter. This must be the case, unless it be possible in reason to say that, for the purpose of including one class of acts which would not otherwise be embraced, a literal construction, although in conflict with reason, must be applied, and for the purpose of including other acts which would not otherwise be embraced, a reasonable construction must be resorted to. That is to say, two conflicting rules of construction must at one and the same time be applied and adhered to.

The obscurity and resulting uncertainty, however, are now but an abstraction, because it has been removed by the consideration which we have given quite recently to the construction of the anti-trust act in the Standard Oil case.

Coming, then, to apply to the case before us the act as interpreted in the Standard Oil and previous cases, all the difficulties suggested by the mere form in which the assailed transactions are clothed become of no moment. This follows because, although it was held in the Standard Oil case that, giving to the statute a reasonable construction, the words "restraint of trade" did not embrace all those normal and usual contracts essential to individual freedom, and the right to make which was necessary in order that the course of trade might be free, yet, as a result of the reasonable construction which was affixed to the statute, it was pointed out that the generic designation of the 1st and 2d sections of the law, when taken together, embraced every conceivable act which could possibly come within the spirit or purpose of the prohibitions of the law, without regard to the garb in which such acts were clothed. That is to say, it was held that, in view of the general language of the statute and the public policy which it manifested, there was no possibility of frustrating that policy by resorting to any disguise or subterfuge of form, since resort to reason rendered it impossible to escape, by any indirection, the prohibitions of the statute.

Considering, then, the undisputed facts which we have previously stated, it remains only to determine whether they establish that the acts, contracts, agreements, combinations, etc., which were assailed, were of such an unusual and wrongful character as to bring them within the prohibitions of the law. That they were, in our opinion so overwhelmingly results from the undisputed facts that it seems only necessary to refer to the facts as we have stated them to demonstrate the correctness of this conclusion. Indeed, the history of the combination is so replete with the doing of acts which it was the obvious purpose of the statute to forbid, so demonstrative of the existence from the beginning of a purpose to acquire dominion and control of the tobacco trade, not by the mere exertion of the ordinary right to contract and to trade, but by methods devised in order to monopolize the trade by driving competitors out of business, which were ruthlessly carried out upon the assumption that to work upon the fears or play upon the cupidity of competitors would

make success possible. We say these conclusions are inevitable, not because of the vast amount of property aggregated by the combination, not because, alone, of the many corporations which the proof shows were united by resort to one device or another. Again, not alone because of the dominion and control over the tobacco trade which actually exists, but because 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, — a purpose whose execution was illustrated by the plug war which ensued and its results, by the snuff war which followed and its results, and by the conflict which immediately followed the entry of the combination in England, and the division of the world's business by the two foreign contracts which ensued. (*c*) By the ever-present manifestation which is exhibited of a conscious wrongdoing by the form in which the various transactions were embodied from the beginning, ever changing, but ever in substance the same. Now the organization of a new company, now the control exerted by the taking of stock in one or another or in several, so as to obscure the result actually attained, nevertheless uniform, in their manifestations of the purpose to restrain others and to monopolize and retain power in the hands of the few who, it would seem, from the beginning, contemplated the mastery of the trade which practically followed. (*d*) By the gradual absorption of control over all the elements essential to the successful manufacture of tobacco products, and placing such control in the hands of seemingly independent corporations serving as perpetual barriers to the entry of others into the tobacco trade. (*e*) By persistent expenditure of millions

upon millions of dollars in buying out plants, not for the purpose of utilizing them, but in order to close them up and render them useless for the purposes of trade. (*f*) By the constantly recurring stipulations, whose legality, isolatedly viewed, we are not considering, by which numbers of persons, whether manufacturers, stockholders, or employees, were required to bind themselves, generally for long periods, not to compete in the future. Indeed, when the results of the undisputed proof which we have stated are fully apprehended, and the wrongful acts which they exhibit are considered, there comes inevitably to the mind the conviction that it was the danger which it was deemed would arise to individual liberty and the public well-being from acts like those which this record exhibits, which led the legislative mind to conceive and to enact the anti-trust act, — considerations which also serve so clearly to demonstrate that the combination here assailed is within the law as to leave no doubt that it is our plain duty to apply its prohibitions.

In stating summarily, as we have done, the conclusions which, in our opinion, are plainly deducible from the undisputed facts, we have not paused to give the reasons why we consider, after great consideration, that the elaborate arguments advanced to affix a different complexion to the case are wholly devoid of merit. We do not, for the sake of brevity, moreover, stop to examine and discuss the various propositions urged in the argument at bar for the purpose of demonstrating that the subject matter of the combination which we find to exist, and the combination itself, are not within the scope of the anti-trust law, because, when rightly considered, they are merely matters of intrastate commerce, and therefore subject alone to state control. We have done this because the want of merit in all the arguments advanced on such subjects is so completely established by the prior decisions of this court, as pointed out in the Standard Oil case, as not to require restatement.

Leading as this does to the conclusion that the assailed combination in all its aspects — that is to say, whether it be looked at from the point of view of stock ownership or from the standpoint of the principal corporation and the accessory or subsidiary corporations, viewed independently, including the foreign corpora-

tions in so far as by the contracts made by them they became coöperators in the combination — comes within the prohibitions of the 1st and 2d sections of the anti-trust act, it remains only finally to consider the remedy which it is our duty to apply to the situation thus found to exist.

The remedy.

Our conclusion being that the combination as a whole, involving all its coöperating or associated parts, in whatever form clothed, constitutes a restraint of trade within the 1st section, and an attempt to monopolize or a monopolization within the 2d section of the anti-trust act, it follows that the relief which we are to afford must be wider than that awarded by the lower courts, since that court merely decided that certain of the corporate defendants constituted combinations in violation of the 1st section of the act, because of the fact that they were formed by the union of previously competing concerns, and that the other defendants not dismissed from the action were parties to such combinations, or promoted their purposes. We, hence, in determining the relief proper to be given, may not model our action upon that granted by the court below, but, in order to enable us to award relief coterminous with the ultimate redress of the wrongs which we find to exist, we must approach the subject of relief from an original point of view.

Under these circumstances, taking into mind the complexity of the situation in all of its aspects, and giving weight to the many-sided considerations which must control our judgment, we think, so far as the permanent relief to be awarded is concerned, we should decree as follows: 1st. That the combination, in and of itself, as well as each and all of the elements composing it, whether corporate or individual, whether considered collectively or separately, be decreed to be in restraint of trade and an attempt to monopolize and a monopolization within the 1st and 2d sections of the anti-trust act. 2d. That the court below, in order to give effective force to our decree in this regard, be directed to hear the parties, by evidence or otherwise, as it may be deemed proper, for the purpose of ascertaining and determining upon some plan or method of dissolving the combination and of recreating, out of the elements now com-

posing it, a new condition which shall be honestly in harmony with and not repugnant to the law. 3d. That for the accomplishment of these purposes, taking into view the difficulty of the situation, a period of six months is allowed from the receipt of our mandate, with leave, however, in the event, in the judgment of the court below, the necessities of the situation require, to extend such period to a further time not to exceed sixty days. 4th. That in the event, before the expiration of the period thus fixed, a condition of disintegration in harmony with the law is not brought about, either as the consequence of the action of the court in determining an issue on the subject, or in accepting a plan agreed upon, it shall be the duty of the court, either by way of an injunction restraining the movement of the products of the combination in the channels of interstate or foreign commerce, or by the appointment of a receiver, to give effect to the requirements of the statute.

Pending the bringing about of the result just stated, each and all of the defendants, individuals as well as corporations, should be restrained from doing any act which might further extend or enlarge the power of the combination, by any means or device whatsoever. In view of the considerations we have stated, we leave the matter to the court below to work out a compliance with the law without unnecessary injury to the public or the rights of private property.

While in many substantial respects our conclusion is in accord with that reached by the court below, and while also the relief which we think should be awarded in some respects is coincident with that which the court granted, in order to prevent any complication, and to clearly define the situation, we think, instead of affirming and modifying, our decree, in view of the broad nature of our conclusions, should be one of reversal and remanding, with directions to the court below to enter a decree in conformity with this opinion, and to take such further steps as may be necessary to fully carry out the directions which we have given.

And it is so ordered.

Mr. Justice Harlan concurred in part and dissented in part:

I concur with many things said in the opinion just delivered

for the court, but it contains some observations from which I am compelled to withhold my assent.

I agree most thoroughly with the court in holding that the principal defendant, the American Tobacco Company, and its accessory and subsidiary corporations and companies, including the defendant English corporations, constitute a combination which, "in and of itself, as well as each and all of the elements composing it, whether corporate or individual, whether considered collectively or separately," is illegal under the anti-trust act of 1890, and should be decreed to be in restraint of interstate trade and an attempt to monopolize and a monopolization of part of such trade.

The evidence in the record is, I think, abundant to enable the court to render a decree containing all necessary details for the suppression of the evils of the combination in question. But the case is sent back with *directions* further to hear the parties, by evidence or otherwise, "for the purpose of ascertaining and determining upon some plan or method of dissolving the combination, *and* of *recreating* out of the elements *now* composing it, a new condition" which shall not be repugnant to law. The court, in its opinion, says of the present combination that its illegal purposes are overwhelmingly established by many facts; among others, "by the ever-present manifestation which is exhibited of a *conscious wrongdoing* by the form in which the various transactions were embodied from the beginning, ever changing, but ever in substance the same. Now the organization of a new company, now the control exerted by the taking of stock in one or another, or in several, so as to obscure the result actually attained, nevertheless uniform in their manifestations of the purpose to restrain others, and to monopolize and retain power in the hands of the few, who, it would seem, from the beginning contemplated the mastery of the trade which practically followed. By the gradual absorption of control over all the elements essential to the successful manufacture of tobacco products, and placing such control in the hands of seemingly independent corporations, serving as perpetual barriers to the entry of others into the tobacco trade." The court further says of this combination and monopoly:

The history of the combination is so replete with the doing of acts which it was the obvious purpose of the statute to forbid, so demonstrative of the existence, from the beginning, of a purpose to acquire dominion and control of the tobacco trade, not by the mere exertion of the ordinary right to contract and to trade, but by methods devised in order to monopolize the trade, by driving competitors out of business, which were ruthlessly carried out, upon the assumption that to work upon the fears or play upon the cupidity of competitors would make success possible.

But it seems that the course I have suggested is not to be pursued. The case is to go back to the circuit court in order that, out of the elements of the old combination, a new condition may be "re-created" that will not be in violation of the law. I confess my inability to find, in the history of this combination, anything to justify the wish that a new condition should be "re-created" out of the mischievous elements that compose the present combination, which, together with its component parts, have, without ceasing, pursued the vicious methods pointed out by the court. If the proof before us — as it undoubtedly does — warrants the characterization which the court has made of this monster combination, why cannot all necessary directions be now given as to the terms of the decree? In my judgment, there is enough in the record to enable this court to formulate specific directions as to what the decree should contain. Such directions would not only end this litigation, but would serve to protect the public against any more conscious wrongdoing by those who have persistently and "ruthlessly," to use this court's language, pursued illegal methods to defeat the act of Congress.

I will not say what, in my opinion, should be the form of the decree, nor speculate as to what the details ought to be. It will be time enough to speak on that subject when we have the decree before us. I will, however, say now that, in my opinion, the decree below should be affirmed as to the tobacco company and its accessory and subsidiary companies, and reversed on the cross appeal of the government.

But my objections have also reference to those parts of the court's opinion reaffirming what it said recently in the Standard Oil case, about the former decisions of this court touching the

anti-trust act. We are again reminded, as we were in the Standard Oil case, of the necessity of applying the "rule of reason" in the construction of this act of Congress,—an act expressed, as I think, in language so clear and simple that there is no room whatever for construction.

Congress, with full and exclusive power over the whole subject, has signified its purpose to forbid *every* restraint of interstate trade, in whatever form, or to whatever extent; but the court has assumed to insert in the act, by construction merely, words which made Congress say that it means only to prohibit the "undue" restraint of trade.

If I do not misapprehend the opinion just delivered, the court insists that what was said in the opinion in the Standard Oil case was in accordance with our previous decisions in the Trans-Missouri and Joint Traffic cases, if we resort to *reason.* This statement surprises me quite as much as would a statement that black was white or white was black. It is scarcely just to the majority in those two cases for the court at this late day to say or to intimate that they interpreted the act of Congress without regard to the "rule of reason," or to assume, as the court now does, that the act was, for the first time, in the Standard Oil case, interpreted in the "light of reason." One thing is certain, "rule of reason," to which the court refers, does not justify the perversion of the plain words of an act in order to defeat the will of Congress.

By every conceivable form of expression, the majority, in the Trans-Missouri and Joint Traffic cases, adjudged that the act of Congress did not allow restraint of interstate trade to any extent or in any form, and three times it expressly rejected the theory, which had been persistently advanced, that the act should be construed as if it had in it the word "unreasonable" or "undue." But now the court, in accordance with what it denominates the "rule of reason," in effect inserts in the act the word "undue," which means the same as "unreasonable," and thereby makes Congress say what it did not say; what, as I think, it plainly did not intend to say; and what, since the passage of the act, it has explicitly refused to say. It has steadily refused to amend the act so as to tolerate a restraint of in-

terstate commerce even where such restraint could be said to be "reasonable" or "due." In short, the court now, by judicial legislation, in effect amends an act of Congress relating to a subject over which that department of the government has exclusively cognizance. I beg to say that, in my judgment, the majority, in the former cases, were guided by the "rule of reason"; for it may be assumed that they knew quite as well as others what the rules of reason require when a court seeks to ascertain the will of Congress as expressed in a statute. It is obvious from the opinions in the former cases, that the majority did not grope about in darkness, but in discharging the solemn duty put on them they stood out in the full glare of the "light of reason," and felt and said, time and again, that the court could not, consistently with the Constitution, and would not, usurp the functions of Congress by indulging in judicial legislation. They said in express words, in the former cases, in response to the earnest contentions of counsel, that to insert by construction the word "unreasonable" or "undue" in the act of Congress would be *judicial legislation*. Let me say, also, that as we all agree that the combination in question was illegal under *any* construction of the anti-trust act, there was not the slightest necessity to enter upon an extended argument to show that the act of Congress was to be read as if it contained the word "unreasonable" or "undue." All that is said in the court's opinion in support of that view is, I say with respect, *obiter dicta*, pure and simple.

For the reasons stated, I concur in part with the court's opinion and dissent in part.[1]

[1] A number of the results following the dissolution are detailed herein at pp. 313 ff., *supra*. W. S. Stevens, Industrial Combinations and Trusts, chapter XIV, reprints both the Standard Oil and Tobacco decrees of dissolution. In his chapter XV he reprints protests of independent concerns as to its efficacy.

XVIII

THE RULE OF REASON APPLIED CONCRETELY, 1911–1915

Two groups of recent Anti-Trust law cases are carried over as a legacy from the preceding chapter because in their final adjudication, the logical consequences of interpretation according to the rule of reason are peculiarly apparent. These are, respectively, those cases which have to do with misuse of the patent laws, and those which embody unfair, that is to say unsportsmanlike, practices. Instances of each abound in the period preceding 1911; but they mark no progress in the unfolding of the law. It is only after the clear cold light of reason has once been turned upon them in the Standard Oil decision, that they become significantly phosphorescent.

Foremost examples of prevented misuse of the patent laws are found in the conviction of John H. Parks in 1908, who was fined $50,000 for organizing a patent pool in the paper trade; and in the condemnation, with penalties of $128,700, three years later of some nine patent pools in the electrical manufacturing business. An umbrella frame combination in 1907, the bicycle coaster brake prosecutions in 1912–1913, and the clothes wringer agreement the following year, alike resemble in principle the Bathtub case of 1913 which is reported first in this chapter. Heavy fines were imposed in each instance and the pool was compelled to disband. Akin to this class of cases, but rather more technical in interpretation, in the light of public interest is the first United Shoe Machinery Company decision of 1914. The lower Federal court found sufficient justification for the monopoly in the patent laws even to overlook what otherwise and elsewhere would have been condemned as unfair practice in making exclusive agreements contrary to the public interest. On the other hand, in the electric lamp pool between the General Electric and Westinghouse companies in 1911, the courts found such elements of public menace as to cause it to be unqualifiedly condemned.[1] The Kodak and motion picture company cases, now pending,[2] still further illustrate the confusing character of combinations, supported on the one side by the public

[1] *Cf.* Stevens in the *Quarterly Journal of Economics*, Vol. XXVI, 1912, pp. 594–602; as also Industrial Combinations and Trusts, pp. 248 and 316.

[2] These, just decided, are discussed in the Introduction to this volume.

necessity of protecting inventive ability, while yet disapproved on the other because of oppressive trade practices which tend to stifle opportunity for others.

Space does not permit of a description of all of the unfair practices which have been disclosed in these anti-monopoly cases.[1] But three of the opinions reprinted in this chapter, namely the Bathtub, the Keystone Watch and the Cash Register cases, serve to show why the legislation of 1914 amending the Sherman Act came to be imperatively demanded by an outraged public opinion. The fundamental point at issue in this group of offences is not merely the immediately evil and oppressive effect of such unfair tactics as espionage, intimidation, local price cutting and the like; but whether in entire absence of such practices, the inherent economies of monopolistic or even sometimes only of very large scale production, are sufficient to perpetuate combination in the face of alert and active competition. The success of such concerns as the International Harvester Company and the U. S. Steel Corporation prove that "big" business is not necessarily unfair business. But the puzzling question then remains as to whether size and power, *per se*, even when avowedly handled fairly, still contain within themselves such seeds of danger, as to warrant judicial condemnation. This is the problem which is discussed in the International Harvester decision in this chapter [2] and in the Steel Corporation opinion in Chapter V.

The Keystone Watch case is illuminating, also, along with the St. Louis Terminal Association decision,[3] as an indication of the wise application of the law since the Standard Oil opinion, in making a distinction between the good and the bad features of a business. Before 1911 a combination must necessarily have been either approved in entirety as to its organization and conduct and allowed to go unmolested, or else have been unqualifiedly condemned and summarily dissolved. But in these instances, it appears that a public policy is possible which shall correct the unwholesome features, and yet leave open the door of enterprise to realize all of the rewards of ability, except those which flow from an arbitrary and unfair exercise of power and advantage. To effect such a distinction between good and evil is, as will appear in the next chapter, the task laid upon the Federal Trade Commission in 1914, acting in coöperation with the judiciary. Not for years has the outlook for industrial peace in the domain of large enterprises looked more hopeful, in consequence of decisions of this sort. — Ed.

[1] Stevens categorically assembles them in *Political Science Quarterly*, Vol. XXIX, 1914, pp. 282–306 and 460–490; and Industrial Combinations and Trusts, chapter XII.
[2] P. 634, *infra*. [3] P. 495, *supra*.

THE BATHTUB CASE[1]

A Patent Pool

The United States brings this suit. It will be called the government. Its petition is filed under the fourth section of the Sherman Anti-Trust Act. It charges that the defendants have violated the first and second sections of that act. It says that they have conspired to restrain interstate trade in sanitary enameled iron ware, and have attempted to monopolize such trade therein. All the defendants are concerned in making and selling that ware. It is made of cast iron. It is coated with enamel. It has the appearance of being porcelain lined. Bathtubs, lavatories, closet bowls, and tanks, sinks, and urinals are among the more important articles made of it. It will be referred to as the ware.

There are 50 defendants. Sixteen are corporations. They will be called the corporate defendants. Thirty-four are individuals. They are styled individual defendants. One of them is Edwin L. Wayman. With him each of the corporate defendants made an agreement. These agreements the government says restrain trade in the ware, and attempt to monopolize it. The other 33 individual defendants are officers of the corporate defendants. The government charges that they each were among the persons who knowingly caused the corporate defendants to do that of which it complains.

Opinion of the Court

These 16 agreements were, with exceptions to be mentioned, identical in their language. At least 15 of the 16 corporate defendants had directly or indirectly taken part in drafting the common form. They were executed by nearly all the corporate defendants on the same day and at the same place. No defendant entered into the agreement without knowing that at least 13 of the other corporate defendants had executed it, or intended so to do. Without this knowledge no one of them would have become a party to it. Each of these agreements is in the form

[1] *U. S.* v. *Standard Sanitary Man'f'g Co.*, Circuit Court, 191 Fed. Rep. 172; 226 U. S. 220; decided October 13, 1911. Omissions are not always indicated.

of a license granted by Wayman accepted by a corporate defendant. The patents under which the licenses purported to be granted were first put into Wayman's name two days before most of the agreements were executed. The terms of the agreements had been definitely settled at least two weeks earlier. There were three patents. They all were for automatic dredgers. A dredger is a tool used in the enameling step of making the ware. The licenses were granted for a period of two years, beginning June 1, 1910. Each licensee promised on the 5th day of each month to pay $5 a day for each furnace used by it for the making of the ware during the preceding month. Wayman undertook that he would three months later pay back $4 out of every $5. This undertaking was conditioned upon the licensee having in the meantime done all he had agreed to do. There are about 25 working days a month. Wayman on the 5th of every month, therefore, received $125 for each furnace continuously operated during the preceding month by any one of his licensees. One hundred dollars of this he was eventually to pay back. This repayment was not to be made until three months had gone by. After the first four months, he would always have in his hands $300 of his licensees' money for every furnace of theirs in steady use. As it actually turned out, he usually held between $40,000 and $50,000 belonging to them. This money was in the nature of cash bail. Each corporate defendant in this manner gave security that he would keep his bargain, or be good, as one of the licensees expressed it. Each corporate defendant promised to do three things: (1) It would not sell any "seconds" or "Bs" of any of the ware except bathtubs. It apparently reserved the right to market what the trade calls "non-guaranteed" bathtubs. (2) It would not sell any ware to any jobber who did not sign the jobbers' resale agreement to be presently described. (3) It would not sell anybody any ware at a lower price or upon more attractive terms than those named in the agreement or in a schedule attached to it. This schedule named standard prices for each article of the ware and for each size, shape, and grade of that article. All the corporate defendants promised that they would not sell some articles below

the scheduled price. Some of them undertook not to sell any articles below these prices. Some of the corporate defendants had not the established reputation of others, or they had not as efficient a selling force. They would not take licenses unless they were allowed to sell some articles at a little lower price than those quoted by their stronger rivals. After much negotiation, it was settled by a committee of the corporate defendants that some of them should be allowed to sell some articles at a discount of 2½ in some instances, of 5 per cent in others, from the scheduled prices. The permission to give this discount, granted to some of the corporate defendants and not to others, was the only respect in which there was any difference among any of the agreements as executed. The negotiation as to which of the corporate defendants should be allowed by the others to give these preferential prices to their customers and how great the permitted discount should be was finished before any of the agreements were executed and before any of the patents had been put in Wayman's name. The resale agreement which the jobber in the ware was required to sign bound him in two respects: (1) He could not buy any ware from any one other than the corporate defendants. (2) He could not sell ware to anybody at a lower price or on more attractive terms than those named in the resale price lists.

The principles upon which these resale prices were to be worked out in detail had been agreed upon between Wayman and a committee chosen by nearly all of the corporate defendants. This agreement was reached before any licenses were accepted, and before any of the patents had become Wayman's. The licenses provided that no changes in the sale or resale prices could be made without the consent of Wayman and the majority of a committee elected by the corporate defendants. The agreements restricted in a number of ways the freedom of both the corporate defendants who made the ware and the jobbers who sold it to the plumbers. An article of the ware must always be billed separately from other goods sold at the same time to the same person. Many articles could not be shipped uncrated. No allowance could be made for a returned crate and so on. There were jobbers to whom these rules or

some of them were distasteful. Dealers were forced to change their methods of doing business which they had followed for years to the mutual satisfaction of themselves and their customers. These requirements had a purpose. Competition in price cannot be altogether shut off unless everybody is made in some respects to do business in precisely the same way as everybody else. Each jobber, like each maker, was called on to give cash security that he would carry out his bargain. He had to pay 5 per cent more for the ware than the maker expected to get out of it. If he had not cut prices and had not bought ware from anyone other than the corporate defendants at the end of the calendar year, he was entitled to receive a rebate of 5 per cent on the amount paid by him during the year. If his purchases from all the corporate defendants combined had amounted to as much as $30,000, his rebate was to be at the rate of 10 per cent. Applications for rebates were to be made to Wayman. When he approved them, they were paid by the corporate defendant or defendants which had sold the applicant the ware. Nearly 400 jobbers signed these agreements. They constituted more than four fifths of all the jobbers in the country. The consumption of the ware is large. Wayman doubtfully estimated the annual value of the national output of it at $14,000,000. It is hardly less than $10,000,000. It may be much more. Upwards of 80 per cent of the jobbers took licenses. They probably handled at least 80 per cent of the product; that is, their total yearly purchases from the corporate defendants must have footed up about $8,000,000. A rebate of 5 per cent on $8,000,000 amounts to $400,000 of 10 per cent to $800,000. Towards the close of every calendar year the corporate defendants would among them hold in the neighborhood of half a million of the jobbers' money. Moreover, the agreements told the jobbers in plain words that, if they cut prices or bought ware from anybody other than the corporate defendants, none of the latter would sell them again. There were jobbers who did not like some of the new rules. Some of them thought their money would be more useful in their own bank account than in that of the corporate defendants. A little less than one fifth of them refused to sign the agreements.

On the other hand, there was from the jobbers' standpoint much that was attractive in the scheme as a whole. Competition had been fierce. It had not always been either wise or honest. A badly made article may look well enough to deceive the average householder. Many such had been put on the market. When the defects were speedily discovered, the jobber might have to take back the article. The cost of doing so ate up the profit on a number of like articles which were not returned. There was little profit in handling the ware. If every dealer signed the agreement, none of them could gain by taking from the makers and putting off on the public any ware except bathtubs, not standard of its kind. The lowest price the makers could take would buy a good article. No one would have a "second" if for the same money he could get a standard. Moreover, while non-guaranteed bathtubs could be sold, the price below which they could not be sold was fixed. The jobbers would therefore insist on getting the best of that not very good grade. With the worst made articles taken out of the market, friction with customers would be lessened. The reputation of the ware would be raised. Every jobber would know that he was buying and selling on the same terms as his competitors. He could tell to the fraction of a cent what his gross profit on every article sold by him would be. He could regulate accordingly his expenditures for handling and advertising it. If he did not take a license, he took large chances. No one of the corporate defendants would sell to him.

Of 250 furnaces in the country the defendants owned 195, or 78 per cent. In drawing building specifications architects frequently called for ware made by a particular manufacturer. A jobber who could not furnish a plumber with what he wanted for a large job was likely to lose his custom altogether. May, 1910, must have been a trying time for jobbers with a stubborn liking for independence, and a taste for managing their own business in their own way. As already stated, in the end four out of every five of the jobbers signed up. Many of them did so willingly and even enthusiastically. It is probable that the large majority of them welcomed the chance of doing so. Their associations had been urging the manufacturers to put in force a resale

arrangement. A number of them have testified that they wanted it. While it lasted, they say they found it pleasant and profitable. In consequence of these proceedings and of other action taken by the government, the corporate defendants on January 1, 1911, suspended so much of the agreements as fixed original and resale prices. Many of the jobbers regret the suspension.

With whatever of enthusiasm, with whatever of reluctance, the makers of nearly four fifths of the ware and more than four out of every five dealers in it became parties to the combination. The corporate defendants, and many, if not most, of the jobbers, were engaged in interstate commerce in the ware. Such commerce was directly restrained by the agreements. The makers who became parties to them could no longer sell the jobbers who did not. The jobbers who did could no longer buy from the makers who did not. The defendants did their best to get all the makers of importance and all the dealers to become parties to the scheme. If they had succeeded, Wayman and a committee of the corporate defendants would for two years from June 1, 1910, have been able to say that no man anywhere in the United States should buy a bathtub or any other article of the ware at a lower price than it might have suited them to fix. If the trade would then have been monopolized, the defendants attempted to monopolize it.

The important questions in the case are two: (1) Would such a combination as was attempted, and in large part brought about, have violated the Sherman Act, had patents on automatic dredgers played no part in it? (2) If it would, did the part played by those patents make lawful what otherwise would have been forbidden?

The defendants argue that not every agreement to fix and maintain prices in interstate commerce violate the Sherman Act. They say that eyes illumined by the light of reason will see that what the defendants did was, from the standpoint of the public interests, good and not evil. They contend that the jobbers were making little profit on the ware. It was troublesome and costly to handle. "Seconds" were on the market. "The ware was getting a bad reputation. If the defendants had not done what they did, there would soon have been no trade either to restrain or to monopolize. There is little in the record to sup-

port this contention. Such an apprehension is vaguely expressed by some witnesses. If there had been marked falling off in the sale of the ware, the defendants know it. They could have shown it by definite and precise figures. They made no attempt to do so. If there was any such danger, it was very remote, far too remote to justify the defendants in doing anything which except for it would have been unlawful. That there was any real danger at all is not shown. According to the defendants, the public gained by what was done even upon the assumption that, if it had been left undone, the trade would have continued in undiminished volume. The ultimate purchaser of the ware seldom knows whether he gets a well-made article. To his eyes it may look well. He may think that it will for years be useful, sightly, and sanitary. In a few months he may find that it is wearing badly, and has become unsightly. He may have reason to fear that to some extent it has become dangerous to the health of himself and his family. He suffers from the greed of the maker, the jobber or the plumber, or of two or all of them. He will be in no danger from that greed when no one of them can any longer make any money by selling him a bad article for the price of a good. Human nature being what it is, no other effective protection can be given him. If the so-called "seconds" and "Bs" are put upon the market at all, most of them will in the end be bought by people who do not know what they are buying. It is useless, according to this argument, to call the makers together and ask them to stop selling such goods. Resolutions pledging all the manufacturers to stop making and selling them, it is true, may be easily passed. They will be adopted with enthusiasm or with solemnity according to the mood of the moment, but always with absolute unanimity. Like so many other gentlemen's agreements, they will be straightway broken.

If an enforceable bargain can be made that no goods shall be sold below a certain fixed price, which will yield a reasonable profit on a first-class article, jobbers and plumbers can be depended upon not to pay that price for an inferior article. The defendants say that in no other way can seconds be taken off the market and kept off. They point to what happened after January 1, 1911, when the price-fixing provisions of the agree-

ment were suspended. The prohibitions against selling "Bs" and "seconds" were still in full force. Nevertheless the defendants' witnesses say that the market was at once flooded with low-grade ware. Much of it came from some of the corporate defendants. It may be better for the public to pay a higher price for better ware. Most individuals find that it is usually cheaper in the end.

Still, two questions remain: (1) Does the law permit the additional price which the public is to pay to be fixed by a combination of dealers even if the latter do so, because they cannot in any other way keep some of their own number from selling bad ware for good? (2) Has the experience of mankind led them to believe that to permit all the makers and dealers in articles of common use to combine to fix the prices and terms below which those goods may not be sold will tend in the long run to improve the quality of the goods?

The second question is not for the courts. The learned counsel for the defendants say that the first need not be answered in this case. They claim that prices were not raised by the defendants. They assert that the evidence shows that they were in fact lowered. The contention rests on a statement of Wayman. He says that the prices as fixed were intended to be on an average about 5 per cent below those named in the last previously published price list of the defendant, the Standard Sanitary Manufacturing Company. The counsel for the defendants in supposing that Wayman meant that he reduced the then actually prevailing prices have misapprehended the market conditions. They assume that the Standard and the other corporate defendants were in fact getting the prices set forth in their catalogue. The record shows that they were not. Whether they ever had does not appear. They certainly had not during any of the period as to which the record speaks. If in the winter and spring of 1910 those prices had prevailed, there would have been no agreements and consequently no case. The agreements as made became fully operative June 4, 1910. No witness says that the published list prices had for many months been generally paid. The evidence is overwhelming that they had not.

On August 4, 1909, Wayman became commissioner or actuary of a newly organized or reorganized Sanitary Enameled Ware

Association. All the corporate defendants, except the Kerner Manufacturing Company, belonged to it. Four other makers of the ware were members of it. These four refused to enter into the price agreements. Consequently they did not take licenses from Wayman. One of his duties as commissioner of the association appears to have been to do what he could by argument and expostulation to prevent price cutting among its members. To this end he wrote many letters. In one of them he speaks of cuts from 2½ to 5 per cent below the published prices as the normal and usual thing. He takes them for granted. They are not cause for complaint. What worries him is the cuts of 20 per cent which he says were then being made. In March, 1910, the terms of the agreements executed two months later were being worked out by correspondence and conferences among the defendants. In that month Commissioner Wayman urged the members of the association to stop quoting what he called the "ridiculous" prices which had recently been made. The Standard Sanitary Manufacturing Company, whose published price lists defendants' counsel suppose show the actual market prices, appears to have had a regularly organized system of rebates. When the agreements now in controversy went into effect, the Standard notified its customers that their special rebates would be withdrawn. They were told, however, that checks would be sent them for whatever rebates were then due. The correspondence between the Standard and another of its customers shows that he had been buying at the "supposed" car load limit price less a confidential 7½ per cent discount. Whether the "supposed" car load limit price was the published price or a generally understood discount below it does not appear.

The record contains many letters written by jobbers to some one or the other of the corporate defendants asking that orders alleged to have been sent in before June 4, 1910, should be filled at the old prices. Sometimes their requests were granted. They were grateful. Sometimes they were told that their order had not come to hand before June 4. If filled, it must be at the new prices. A long correspondence usually followed. The jobber tried hard to get the ware at the old price. Many letters passed between one Sullwold and the defendant Ahrens. Ahrens is

president of the Standard. Sullwold is head of a Minneapolis jobbing house. He did not like the new scheme. Ahrens tried to get him to come into it. They wrote each other at great length. They go into many details. Whenever one thinks he can make a point on the other, he does so. Sullwold repeatedly says that the ware will cost the jobbers more. Ahrens does not deny. Both take it for granted. Wayman testifies that to stop "ruinous competition" was one of the purposes of the agreements.

The J. M. Kohler Sons Company of Sheboygan, Wis., was a member of the Sanitary Enameled Ware Association. Wayman and a number of the defendants worked hard to get it to take a license. It would not. It claimed that the scheme was a price agreement, pure and simple. It said that price agreements were forbidden by the laws of the United States and of Wisconsin. One Kroos is connected with it. He was a witness for the government. He presented some elaborate calculations as to the difference between the prices his company had been getting for the ware and the prices it would have received under the Wayman plan. As he figured it, the latter were in every instance greater. The difference ranged from 1 to 45 per cent. Defendants' counsel say that he did not know what he was talking about. According to them, he did not understand how the price tables of the defendants were to be applied. He, however, gave the prices of his own company for the various articles principally dealt in by it and the defendants. It would have been easy for the latter to show what the true comparison was, if it had seemed to them expedient so to do. It is, however, not important to determine whether Kroos did or did not fall into error. There is in the record a letter to the Standard Sanitary Manufacturing Company from one of its customers. It was written shortly after the price agreements went into effect. In it the writer remarks that, of course, the Standard understood that he could not do much with their prices so long as Kohler continued to sell at the prices it was then making. Quite clearly the new prices were materially higher than Kohler's. The record shows that the agreements were intended to raise prices, and that they did so. How great the increase was is not shown either in percentages or in dollars and cents. To have figured it out

would have taken much time and money. Very likely no one knows how much prices were raised. Each defendant knows how much more it took in under the agreements than it had obtained before. No one of them had any accurate knowledge as to the gain made by any one of its fifteen corporate codefendants. Not every one of them would have found it easy to tell what the precise percentage of increase in the price received by it for each kind of article had been. Before the agreements went into effect, there was no fixed price. In every large transaction and in many that were not large the price actually paid was the outcome of a special and usually of a secret bargain.

Not only did the agreements raise prices — they prevented reductions that would otherwise have been made. The market conditions in the winter and spring of 1910 were such that prices left to themselves would have gone still lower. How rapidly the drop would have run into money is shown by a statement of the president of the Standard. He was trying to get the Kohler company to take a license. He pointed out how good a thing the scheme was from the manufacturer's standpoint. He said, if it did not go through, it would cost the Standard's stockholders $300,000 in 1910, for in that event he would have to reduce prices. The defendants say that prices may be too low for the public good. Competition may be carried far enough to hurt everybody concerned. It may in the end be the direct cause of monopoly. Under its stress all but the strongest producers may go to the wall. The government replies that, if all the makers of an article of common use combine to raise and maintain prices and to punish any one of their number who reduces them, all the evils which to common experience of mankind result from monopolies will surely follow. Possibly both the defendants and the government speak truly. It may be that one of the great problems of the day is to find some way of protecting the general public against monopolistic combinations without compelling business men to subject themselves and their capital to all the perils of unrestrained competition. To find its solution would appear to be the business of the statesman. The defendants say the courts may give it. In their opinion makers and dealers may combine to raise prices

without violating the Sherman Act, provided that the prices fixed by their agreement are not unreasonably high.

In each particular case upon the evidence submitted the courts must say whether the prices asked are or are not reasonable. It would not be an easy task. Some standard of reasonableness would have to be worked out. The factors to be taken into account would be numerous and complex. The labor and expense of finding out what all the relevant facts were would be enormous. After all was done and said, the margin of doubt would usually remain large. If the dealers were bound to show affirmatively that their prices were reasonable, the government would usually win. If the government had to show that they were unreasonably high, it would ordinarily lose. In this case the defendants assume that the burden of proof as to the unreasonableness of their prices is on the government. They say, and say truly, that the government has neither shown nor attempted to show that the schedule prices were unreasonable. The government replies every agreement to fix prices and to force or bribe makers or dealers to maintain them is illegal. In its view there are no circumstances in this case which take it out of the general rule. The presumption of law is that the prices which have been made by the free and untrammeled trafficking of the market place are the reasonable prices. Any one who interferes with the natural action and interaction of this bargaining assumes the burden of showing that what he did was fair and reasonable. If such a burden rests on the defendants, it has not been sustained. They had not shown what capital they have invested in the business. They have not told what net profit, if any, they earned under the old prices.

These opposing contentions raise questions of great moment and of exceeding difficulty. To answer them wisely may require going to the very roots of our conceptions of what the relation of the state to the industrial life of its people should be. Every one has the right to discuss them. It may be a duty to do so at all reasonable times and in all proper places. This opinion is not a proper place for such a discussion. Some men believe that price agreements should be sustained by the courts, unless they are shown to be against the public interest. Others hold

that they may be permitted only when it is affirmatively shown that they promote the public interest. Still others say that a price agreement pure and simple is always illegal. That the Supreme Court has declared the last of the above-stated contentions to be the law is conclusive here. Only a few months ago it said:

Agreements or combinations between dealers, having for their sole purpose the destruction of competition and the fixing of prices, are injurious to the public interest and void. *Dr. Miles Medical Co.* v. *John D. Park & Sons Co.*, 220 U. S. 408, 31 Sup. Ct. 384, 55 L. Ed. 519.

[2] At the moment we are considering only one question, Would the agreements have violated the Sherman Act had the dredger patents had no part in them? They destroyed competition. They fixed prices. For that purpose they were made. They had no other. Defendants say that to fix prices and to destroy competition would have been to their profit and to the public good. They may not break the law because they think that it will be well to do so. In view of the character of the parties, the necessary effect of the agreements was clearly to restrain trade within the purview of the statute. In such case they cannot be taken out of the category of the unlawful by general reasoning as to their expediency or non-expediency or the wisdom or want of wisdom of the statute which prohibited their being made. When the nature and character of the contracts create a conclusive presumption bringing them within the statute, such a result is not to be disregarded by the courts by a substitution of a judicial appreciation of what the law ought to be for the plain judicial duty of enforcing the law as it is. *Standard Oil Co.* v. *United States*, 221 U. S. 65, 31 Sup. Ct. 502, 55 L. Ed. 619.

It follows from what has been said that, unless protected by the terms or the policy of the patent laws, the agreements violate the Sherman Act.

[3] 2. Did the part played by the patents make lawful what was otherwise forbidden? The ware is made of cast iron. After it has been shaped, it is enameled. Enameling involves two distinct processes. In each there are several steps. The ware is first given what is called the "slush" coat. This is enamel

applied in liquid form. It is burnt on the base by the application of intense heat. The article is placed in a furnace. It is raised to a red heat, say 1500 degrees Fahrenheit or upwards. It is taken from the furnace. While it still glows, powdered enamel is sprinkled upon it. It is put back in the furnace. It is again heated. When it is taken out, it usually is again sprinkled with the powder. If so, it is again reheated to fuse the enamel upon its surface. This process may be repeated indefinitely. Ordinarily two coats of the powder suffice. When the last has been burnt on, the ware is allowed to cool. It is ready for finishing, inspection, cleaning, shipment, and sale.

The patents spoken of in this case are for automatic dredgers. A dredger is used to sprinkle the powdered enamel on the ware. It serves no other purpose. It is not used in making the iron, or the ware out of the iron, or the liquid, or the powdered enamel, nor in the construction, the heating, or operation of the furnace, nor in taking the weighty and red-hot metal out of the furnace and putting it back. In the doing of these things many compositions of matter, machines, tools, appliances, and processes are employed. Upon the well doing of every one of them the usefulness, the attractiveness, and the durability of the ware depend. Whether any one of them shall be well or ill, cheaply or expensively done, turns in greater or less degree upon the fitness and adaptability of the compositions, machines, tools, appliances, and processes used. Any patentable improvement in any one of them would bear the same relation to the ware as is borne by the automatic dredgers. There might be differences of degree in either direction. In legal theory no distinction would be possible. From this point of view further inquiry into the precise degree of usefulness of the automatic dredger in the sprinkling step of the enameling process of making the ware might be omitted.

The question of law will be, in any event, whether the owner of a patent on one of many tools used in the making of a particular kind of unpatented ware may lawfully make such agreements with reference to it as those in the record. This case is, however, one of importance. In certain respects it is suggested that it is one of the first impressions. It will be well, therefore, to understand how the enameler would like to sprinkle the powder,

and to what extent and in what way the automatic dredger helps him to do it as he would. He wants to use little powder. It is more or less costly. The thinner the enamel coat, the better the ware looks and lasts. The whole surface of the article must be covered; otherwise it will be almost or altogether useless. The more uniform the coat of enamel is, the more sightly and durable it will be. If little powder is to fully cover the entire surface, it must be applied in a finely divided form. Every portion of the surface must receive as nearly as may be precisely the same amount of powder as any other portion of like extent. The sprinkling must therefore be done with great evenness and regularity. It must be done quickly. The powder will not attach itself firmly to the base, unless fused upon it. If every minute portion of the surface is to be covered, the powder must melt and run in liquid form the moment it touches the article. The sprinkling must consequently be done and finished while the iron remains hot enough to liquefy the enamel the instant the latter touches the former. For this purpose a minimum temperature of 1200 degrees Fahrenheit is required. It is true that, if time does not suffice to sprinkle the powder over the entire surface, the article may be returned to the furnace and reheated. When taken out again, the uncovered portion may be sprinkled. A coat applied in installments does not usually look well to an expert eye. It is costly. So to put it on takes more time and more fuel. The manufacturer likes the processes used in his factory to be of a kind easy for the workman to learn and to practice. Labor then costs less both in money and worry.

When makers of enameled ware first wanted to sprinkle powder on iron, they set about doing it in the way in which men had for countless centuries been wont to sprinkle powder for other purposes. They took an ordinary sieve, dredge, or sifter. It was not unlike in size and shape that with which housewives had for time out of mind sifted flour or meal. The enameler, it was true, could not handle his sifter as his wife handled hers. He could not stand beside the surface he was to cover, and with both hands shake the dredge over it. He could not because that surface was a part of a mass of red-hot iron. He must stand back from it. Accordingly a handle was put on the

dredger. He could not shake it as his wife shook hers. Her only object was to reduce the meal to a fine powder. It made no difference whether more of it fell upon one portion of her board or pan than on another. He must sprinkle his powder uniformly. He could not force it through the meshes by moving the whole dredger and its contents more or less briskly back and fro. He must move it regularly and in one direction. It was not desirable to let it come back on its own tracks. The enameler shook his sieve by tapping upon the handle with a piece of iron. This tapping occupied one of his hands. He had to support and guide the dredger with the other. He had a disagreeable choice to make. If he used a dredge with a short handle, he had to stand very near large articles of glowing iron. If he lengthened the handle, the weight of the dredger and its contents, at the end of so long a lever became too great for his strength. What he in fact at first did was to use a dredger with a handle three or four feet long. This brought him very close to the red-hot metal. To partially protect himself from the heat he wore asbestos masks, gauntlets, and breastplates. Even so he had an uncomfortable job. The heat was always disagreeable. At times it must have been trying. Supporting the dredger with six to eight pounds of powder in it, and moving it steadily, firmly, and accurately over the surface, was hard work. Continuously tapping with the other hand was racking to the muscles and nerves, although the force required to give a single tap was doubtless trifling. Not every man was physically able to handle a dredger under such conditions. Few men could have handled it for more than a few minutes at a time. They did not have to. Bathtubs are the largest articles usually made. Defendants' witnesses say that, when the short-handled dredger was used, it took on an average about four minutes to cover a bathtub with the powder. The same witnesses tell us that an expert enameler could enamel some 11 tubs in a working day of ten hours. Each tub ordinarily was given two coats of the powdered enamel. An enameler, therefore, in ten hours went twice over each 11 tubs; that is, he sprinkled 22 coats in all. It took him 22 times four minutes to do it, or eighty-eight minutes in the aggregate. In the ordinary course

of his work he handled the dredger for four minutes. He did something else for 23, then took another four-minute turn with the dredger, and so on throughout the day. It may be that defendants' witnesses have underestimated the number of tubs formerly enameled by a good workman in a single day. Even so, the enameler used the dredger for short intervals only. There were relatively long intermissions when he did not. If it had been otherwise, the incidents related as to the exhaustion and almost collapse of the workmen could have been common and typical, instead of being occasional and altogether exceptional, as they doubtless were. Had they been ordinary occurrences, the industry could scarcely have been carried on.

Whether they were or were not frequent is now immaterial. Before the first automatic dredger was invented, it had ceased to be necessary for the enameler to stand close to the glowing metal or to support the weight of the dredger and its contents. It had occurred to some one that the handle might be supported from the ceiling. It could easily be balanced by a counterweight. The length of the handle was no longer limited by the physical strength of the workman. It was made 7 or 8 feet long. The asbestos armor was discarded, except upon the arm and hand most exposed. The enameler had no great weight to support. One arm could be devoted solely to guiding the dredger. The other was still necessarily occupied in keeping up a continuous tapping. This form of dredger had come generally, if not universally, into use before the invention of the pneumatic dredger some twelve or thirteen years ago. In essence the patented dredgers differ from the unpatented in one respect only. In the former the tapping is done by machinery. In their predecessors it was done by hand. The handle of the patented dredger is made of hollow metal. In it a plunger is fitted. By compressed air or by electricity the plunger is made to keep up a continuous and perfectly steady and uniform tapping. The workman by the pressure of his thumb may at his will increase or decrease the frequency of these tappings, or he may stop them altogether. The automatic dredgers were supported in the same way as the unpatented long-handled dredger had been. The enameler who works with one can use

both hands to guide the dredger. He has nothing else to do. His work is much simplified, and made far easier and more agreeable. The use of both hands gives him a better and a surer control over the motion of the dredger. There is less danger of his putting too much powder in one place and too little in another. Personally he is much more comfortable. He can work faster. At the same time he no longer feels rushed or driven. He knows now that he can put one coat on before the metal cools. Before he was not always, perhaps not usually, sure that he could. As a rule his work is now better done.

The patented dredger was useful in other ways. It could be fitted with a finer mesh. It puts the powder on the metal in a more finely divided form. This, as has been already pointed out, is an advantage. So long as the tapping was done by hand, the blows upon the handle would not always be hard enough to force the powder through a mesh as fine as that which may now be used. The powder falls from an automatically tapped dredge with a regularity and uniformity greater than that which can be given to it by the average workman. The use of patented dredgers may or may not save enameling powder. There is testimony both ways. With such dredgers more work can be done in the same time. Other things equal, it is probable that ware, in the enameling of which they have been used, will on the average be somewhat better enameled than it would have been had hand dredgers been employed.

The record does not enable us to tell in either absolute or relative figures or percentages how great is the saving of time or the bettering of quality. The same number of men in the same time now usually turn out more work than they formerly did. In the attainment of this end the patented dredger helps. Other things contribute. Some, but not all, of these other improvements can be used to greater advantage in connection with the automatic than with the hand dredges. How much the use of the patented dredges improves the quality is still harder to figure out. Some men with fine tools cannot do as good work as other men with poor. The defendants' evidence seems to show that the percentage of ware of high quality turned out depends much more largely upon shop management and efficiency

than it does upon the use of one form of dredger rather than another. One of the defendants' witnesses says that with the hand dredge his shop made 95 per cent of second and only 5 per cent of first class goods. With the automatic dredger he gets 25 per cent of seconds and 75 per cent of firsts. This is definite enough. Another witness for the same side, but whose experience has been had in another factory, says that with the old hand dredge he made only 5 per cent of seconds. By the use of the automatic dredger he has brought that proportion down to 1 per cent. If each of these witnesses is even approximately accurate, it follows that one of them with an automatic dredger made five times as large a proportion of inferior goods as did the other when using a hand dredger.

All that can be safely said is that the automatic dredgers are useful tools. By their use, all other things being equal, ware can be made more cheaply and on the whole of a somewhat better average quality. No one claims that he can tell by inspection of a completed article whether the enameling powder was sprinkled upon it with a hand or an automatic dredger. Some of the witnesses think that, if they were shown two considerable lots of the ware in the enameling of one of which one kind of dredger had been exclusively used and in that of the other another kind, they could say upon which the powder had been shaken from a hand dredger, and upon which from an automatic dredger. It does not appear that the experiment ever has been tried. It is quite probable, nevertheless, that the distinction could frequently be made with reasonable accuracy, provided that the two lots had both been made in the same shop by the same men and under otherwise like conditions, except as to the dredger used. The difference of results attained in different shops as shown by the record, and the further fact that, as soon as the operation of the price restrictions was suspended, some of the defendants, although using the automatic dredger exclusively, put large quantities of seconds on the market, seem to show that it is unlikely that any one could tell upon which of two lots of the ware made in different shops or in the same shop under different conditions the hand dredger had been used and upon which the automatic.

It follows that there is no respect in which every tub in the enameling of which an automatic dredger has been used differs from every tub in the enameling of which the hand dredger has been employed. Whether the ware shall be well or ill made, whether it shall be durable or the reverse, whether it shall be sightly or unsightly, depends upon many circumstances of which the kind of dredger used to sprinkle the powder is only one, and probably not the most important. Much turns on the composition of the enamel. Each factory makes it according to its own formula, which it tries to keep secret. Perhaps none of the powders in use give complete satisfaction. Experiments for their bettering are continually being made. How controlling a part the composition of the powder plays is shown by the account given by one of the defendants' witnesses of the disastrous results upon the ware of an experimental change in the powder made since the first of the present year by one factory. The liquid enamel or slush coat must be properly made and fittingly applied. The furnaces must be adapted to the work to be done by them. The appliances for putting the ware into the furnace and for taking it out again must be constructed, so that with little consumption of time and labor the work will be done without damaging the delicate enamel not yet firmly fused upon its base. The castings must be well made and of the right kind of metal. It is quite possible that a new tool, appliance, or process may be invented for the better doing of any one of them. Its use may improve the average quality or cheapen the average cost of the ware, or both. Every such an inventor, if he obtained a patent for his invention, would be as much entitled as Wayman to say at what price and upon what terms men might deal in the finished article in some stage of the making of which his invention had been used.

Defendants say that while it is true that the automatic dredger is a mere tool, used in only one operation of a number required for the making of the ware, and while it is conceded that merchantable ware can be made without its use, still the advantages of using it are so great that as a commercial proposition the ware cannot be made without it. It is unnecessary to consider what legal consequences, if any, would follow if the

record sustained this claim. It does not. It is true certain witnesses say that in their judgment the automatic dredgers have become necessities for the manufacture of the ware for commercial purposes. The record conclusively demonstrates that they are mistaken. Such concerns as the J. M. Kohler Sons Company and the Iron City Sanitary Manufacturing Company have no rights under any of the patents. There is no evidence of their having infringed them. They make and sell the ware in large quantities in competition with the licensed manufacturers. Moreover, if the experience of the concerns which had the right to use the patented dredger had convinced them that the ware could not without their use be made good enough and cheap enough to be sold in competition with them, it is not conceivable that they should have gone to all the trouble they did to induce those two concerns to take licenses. According to the defendants' present theory, the refusal to do so was tantamount to commercial suicide. If factories without licenses could not make ware which could be sold in competition with that made by those who had licenses, the fewer who had licenses the better for those who had.

The ware is absolutely unpatented. Any one may sell it as freely as he may a loaf of bread. No one can tell by looking at a bathtub whether enameled powder has been sprinkled upon it by a patent dredger any more than any one who eats a loaf of bread can tell whether it has been baked in an oven with a patented grate, or who lights a kerosene lamp can tell whether in the process of refining a patented tool has been used, or by taking a pinch of snuff can be sure that there was or not a patented mill used in grinding the tobacco.

If agreements in this case are not violations of the Sherman Act, similar agreements among all the bakers of bread, the refiners of petroleum, the grinders of snuff will be legal, provided that somewhere in the process of making the bread, refining the petroleum, or grinding the snuff a patented tool has been used. The issue is important. It cuts deep. The record squarely presents it. It must be passed upon. The defendants say they have broken no law, even if all that has thus far been said herein be true. They rely upon what they understand to have

been decided by the Circuit Court of Appeals of the Seventh Circuit in the case of *Rubber Tire Wheel Co.* v. *Milwaukee R. W. Co.*, 154 Fed. 358, 83 C. C. A. 336. There the court said that no one can use a patented article without the consent of the patentee. He may fix his own conditions. It adds:

> Whatever the terms the courts will enforce them provided only that the licensee is not thereby required to violate some law outside of the patent laws, like the doing of murder or arson.

The defendants ask: "Is not the legal title to the dredger patents in Wayman?" "May any use the automatic dredgers without his consent?" "May he not make what terms he will for his license to use them?" "Will not the courts enforce those terms, provided they do not call for the violation of some law outside the patent law, like murder or arson?" "Have the defendants committed murder or arson or anything like either?" Making a price agreement differs widely in many fundamental respects from either murder or arson. The difference is so profound that it can be easier felt than accurately defined. It is not to be found in the circumstance that almost all races of men have for countless centuries felt that murder and arson were highly immoral acts. It would not be difficult from the text of the criminal codes of many different peoples at widely separated periods of the world's history, and from the writings and sayings of ethical and religious teachers of divers creeds and races, to argue that for some thousands of years the vast majority of mankind has felt that it was also immoral to make a combination for the purpose of raising the prices of things of general use. At all times there has been a minority of shrewd and able men who have believed that such combinations were merely the reasonable exercise of superior sagacity and foresight. There never has been a time when most men, however much they disliked price agreements in things they bought, but did not sell, were not able to persuade themselves that there was nothing wrong in agreeing to keep up the prices of things they sold, but did not buy. It is not for us to say what the true ethical relation of the monopolist to the community in which he lives is. In this country those who believe

that he is a dangerous wrongdoer have in lawful manner written their convictions upon the statute book. The Sherman Act forbids restraint of interstate trade and attempts to monopolize it. He who does either may be punished, and that, too, in a way which the Legislature seldom directs, unless the thing forbidden is felt by the majority of the people to be unethical if not highly immoral. The use by the Circuit Court of Appeals of the Seventh Circuit of murder and arson as illustrations of breaches of law which a patentee had no greater immunity to commit than had any other man was accurate, natural, and striking. At a glance, every one could see that a patentee could not lawfully require his licensee to commit either. Unfortunately some people have persuaded themselves that those illustrations were intended as limiting the violations of law which a patentee could not require to crimes which the ordinary man feels to be of the same general type as murder and arson. Such, of course, was not the intention of the court.

A patentee may not require his licensee to sell a patented oil which flashes below the minimum temperature prescribed by state law. *Patterson* v. *Kentucky*, 97 U. S. 501, 24 L. Ed. 1115. He may not authorize his licensee to prescribe and sell his patented medicine in a state which requires of all who write prescriptions that they shall have qualifications not possessed by the licensee. *Jordan* v. *Overseers of Dayton*, 4 Ohio, 295. Selling oil with a low flashing point or prescribing patent medicine without having a state license to practice medicine would no more strike the average man as akin to murder or arson than would a combination to fix prices. In one respect they are like murder and arson. They are violations of law outside the patent laws. So is a combination in restraint of trade. What the court meant was what the court said — a patentee cannot require his licensee to violate a law outside of the patent law. Murder and arson are outside the patent law. Every obligation which a patentee attempts to impose upon his licensee to break any law outside of the patent law is in that respect like a requirement to commit murder or arson. In the nature of things such must be the law. A patentee is as much subject to the laws of the land as is any other man. From one

special application of one class of laws he is exempt. At common law and by statute monopolies are unlawful. At common law and by statute a man who invented a new and useful thing might be given a right which would enable him for a limited time effectually to monopolize it. The courts have said that this right to monopolize what he invented cannot be taken from a patentee by state laws. They say it has not been taken away by Congress. All men know that Congress never intended when it passed the Sherman Act to change the patent law. It did not do so.

The patentee may, in spite of that law, monopolize for the term of his patent the thing which he or his assignor invented. Neither at common law nor in this country by statute has he ever had a right to monopolize anything else. As to everything not validly claimed in his patent he is as other men. If by the common law or the statutes of the state or by the enactments of Congress men are forbidden to restrain trade or to monopolize it, a patentee may not restrain trade or attempt to monopolize it in anything except that which is covered by his patent.

[8] A patent is a grant of a right to exclude all others from making, using, or selling the invention covered by it. It does not give a right to the patentee to sell indulgences to violate the law of the land, be it the Sherman Act or another. The right to exclude others is the property of the patentee. It is his very own. He may do with it as he will. A very rich man may have $100,000,000 of cash. It is his property. It is his very own. He may do with it as he will. Neither one of them can use his property to bring about a violation of law. A patentee who monopolizes his invention breaks no law. He who uses his property right to exclude others from the making, selling, or using his invention, for the purpose and with the effect of making a combination to restrain trade in something from which his patent gives him no right to exclude others, does break the law. He breaks it precisely as the individual defendants in the Standard Oil and American Tobacco companies broke it. They had the same right to use their brains, their capital, and their credit as they thought best, as he had to use his right to exclude all others from making, using, or selling automatic dredgers.

He was subject to the same limitations as they were. They could not lawfully use their brains, their money, and their credit to restrain trade in petroleum and tobacco. He cannot use his patent rights to restrain trade in unpatented bathtubs.

The defendants have pressed upon our attention many cases in the Circuit Courts and in the Circuit Courts of Appeal. Many of them have upheld the right of a patentee to fix the price below which a purchaser from him of patented articles may not sell those articles. In some of these cases it has been held that one who sells at a lower price thereby becomes an infringer, and that the federal courts have jurisdiction of a suit brought against him on account of such sale, irrespective of the amount in controversy or the citizenship of the parties. The Supreme Court has in several recent cases expressly said that it was not to be understood as expressing any opinion as to whether such restrictions when applied to patented articles were or were not valid. Wayman did not sell patented dredgers on condition that the purchasers should not resell them below a fixed price. The question of whether such restrictions upon the sale of patented articles are valid is not before us. We neither decide it nor intimate any opinion upon it.

In a number of cases the owner of a machine patent has licensed others to use the machine on condition that they would buy certain unpatented things upon which the machine operated exclusively from the patentee. Those conditions have been held valid by a number of courts. Persons who with the knowledge of the terms of the license have sold to the licensee some of the unpatented things to be used on the patented machine have been held liable for contributory infringement. A patentee may or may not be entitled to obtain his pay for his patented machine in whole or in part by stipulating that he shall have the sole right to furnish material to be used with it. We express no opinion upon the question. It would have been presented in this case had Wayman bargained with the corporate defendants that they should buy all their enameling powder from him. Such a bargain would have been a very different one from that now before us. The purposes aimed at by such a bargain, the relations among the defendants, and between them and

the public would have all been unlike those shown in the record.

What has been said is sufficient for the determination of this case. The ware is not patented. The agreements or licenses attempt to fix the price of unpatented ware and to monopolize the trade in it. The fact that Wayman had a patent on something else, even though it was a tool used in one step of the making of the ware, gives neither him nor his licensees the right to restrain interstate trade in the ware. The ownership of a patent for a tool by which old, well-known, and unpatented articles of general use can be more cheaply made gives no right to combine the makers and dealers in the unpatented articles in an agreement to make the public pay more for it. The first and second sections of the Sherman Act, "when taken together, embraced every conceivable act which could possibly come within the spirit or purpose of the prohibitions of the law without regard to the garb in which such acts were clothed. . . . In view of the general language of the statute and of the public policy which it manifested, there was no possibility of frustrating that policy by resorting to any disguise or subterfuge of form, since resort to reason rendered it impossible to escape by any indirection the prohibitions of the statute." *United States* v. *American Tobacco Co.*, 221 U. S. 181, 31 Sup. Ct. 648, 55 L. Ed. 694. In what has been said it has been assumed that Wayman was the real and substantial owner of the patents. That scheme was his. That his purpose was merely to make money for himself by selling to the corporate defendants indulgences to sin against the Sherman Act.

The government contends that this was not the real situation. In its view there is nothing before the court except an ordinary combination to raise and maintain wholesale and retail prices and to force all the makers and dealers in the country into it. Wayman, it says, was nothing more than the ordinary promoter. The patent served the purpose of the certificate of incorporation from New Jersey or Delaware used when the combination became a consolidation. We have not discussed this branch of the case. We will not. We refrain from doing so not because it would not be pertinent. It would. Ordinarily it would receive

full consideration. Unusual circumstances shown by the record make it inexpedient and even improper to do so, if the case can be disposed of without commenting upon that aspect of it.

[5] Some months after these proceedings were begun the grand jury of the United States for the Eastern District of Michigan returned indictments against many of the defendants. They were charged with violating the Sherman Law. The acts alleged against them there are the same which are made the ground of the equitable relief here asked for. The defendants have moved that further proceedings herein be put off until the criminal case has been finally disposed of, and that the taking of testimony be then reopened. It is urged that the individual defendants should in justice to themselves testify fully and freely. It is said that this they dare not now do. They fear that something to which they swear in the civil proceeding may be used in the criminal to their hurt. This motion we cannot grant. The Sherman Act provides for both civil and criminal proceedings. The Attorney-General must decide whether and when either or both shall be brought. To postpone finding an indictment until after a petition for an injunction had upon final hearing been granted or dismissed would be frequently, if not usually, to wait until after the period of limitations had expired. To refuse to decide the equity cause so long as the criminal charge had not been finally disposed of might leave the public to suffer for years from what the Attorney-General believed to be a harmful interference with its rights and interests. The courts cannot, unless in exceptional cases, say that either must wait upon the other. A court of equity has a wide discretion. There may be circumstances which would justify its refusal finally to act until after the indictments had been tried. In our view such circumstances are not found here. The fact that many of the defendants are now under indictment makes it our duty to be careful not to say anything which might be used either to their prejudice or to that of the government in the impending criminal trial. Some minor questions affecting particular defendants are to be passed upon.

[6] The Colwell Lead Company says it is not engaged in interstate commerce. In our view it is. It makes its ware in

New Jersey. It sends it to warerooms in New York City and in Worcester, Mass., and there sells it. Its trade extends over several states. It alleges that it had no part in any of the negotiations leading up to the formation of the scheme, that it did not execute a license agreement until some three weeks after the other corporate defendants, and that, then, it refused to bind itself to charge the resale prices. It was consulted through its president some time before any of the agreements were actually entered into or before their precise terms were definitely settled. He then gave a general approval of the plan. Neither he nor it appear to have done anything further until after the others had signed up.

Some months before the Standard Sanitary Manufacturing Company, which until May 4, 1910, owned the basic automatic patent, had given the Colwell company a revocable license to use the dredger. The latter wanted Wayman to renew the license. It apparently did not want it badly enough to be willing to bind itself to charge the uniform resale prices of the New York City plumbers to whom it sold a large part of the ware. Wayman finally agreed in writing that, if it would take a license, he would try to get from the commission of the corporate defendants leave to cut these prices whenever it found that maintaining them would seriously handicap it. If the commission would not let the Colwell Lead Company do so, the latter on 10 days' notice could terminate the agreement. It would appear that it became a party to the combination to an extent sufficient to entitle the government to injunctive relief against it.

[7] The evidence shows that two of the individual defendants, namely, Bert O. Tilden and George W. Franzheim, secretaries of the Colwell Lead and the Wheeling Enameled Iron companies, respectively, had no part in forming the combination. They did not do anything in connection with it, except to attest in their official characters papers executed by their corporations. As to them the petition should be dismissed. Against the other defendants, corporate and individual, the government is entitled to injunctive relief substantially as prayed for. In view of the pendency of the criminal case, all characterization

of what the defendants have done not necessary to the effectiveness of the decree should be omitted from it.

Goff, Circuit Judge (*dissenting*).

I cannot assent to the conclusion reached by the court in this opinion. The facts established by the testimony, considered in the light of the law applicable thereto, compel me to conclude that the allegations of the petition have not been sustained.

THE INTERNATIONAL HARVESTER CASE[1]

A Well-Behaved Combination

"This case is one of fact, not of controverted questions of law."

On June 24, 1902, P. D. Middlekauff secured, in his own name, an option on the stock and plant of the Milwaukee Harvester Company for $3,123,691.90. He did this in fact as agent, though it does not clearly and certainly appear who his principal was, whether J. P. Morgan & Co., George W. Perkins, or the McCormick Harvesting Machine Company. He did it, however, at the direct instance of the McCormick Harvesting Machine Company, but whether it was acting as principal or agent is left in some slight doubt.

On June 25, 1902, Mr. Middlekauff went to New York with a letter from an officer of the McCormick company, authorizing him to assign this option to J. P. Morgan & Co., of which George W. Perkins was a member, or to any one they might designate, and reciting that the option had been obtained "for us." Mr. Middlekauff remained in New York until July 30, 1902, aside from being absent a small portion of the time in Philadelphia and Washington on busines for Mr. Perkins.

On August 11, 1902, a new contract was made for the purchase of the Milwaukee Harvester plant by Mr. Middlekauff, and on the same day he assigned his contract to Mr. William C. Lane, a New York banker and then president of the Standard Trust Company.

[1] *U. S.* v. *Int. Harv. Co.;* District Court; 214 Fed. Rep. 987; decided August 12, 1914. Economic details in chapter IX, *supra*. Many omissions not indicated.

In July, 1902, the representatives of the McCormick, the Deering, the Warder, Bushnell & Glessner, and the Plano were all in New York, but stopping at different hotels and not seeing one another. They were all seeing, however, Mr. George W. Perkins. On July 28, 1902, they met and gave separate contracts to William C. Lane, heretofore referred to, and his assigns, to sell all their tangible property and specified portions of their bills receivable. These agreements all contained a recital that the purchaser, upon his acquisition of the property, intended to transfer the same to a corporation to be organized under the laws of Illinois, or some other state, called the "purchasing company." It was in each case, except that of the Warder, Bushnell & Glessner Company, stipulated that the entire purchase price should be paid in fully paid non-assessable stock of the purchasing company.

On August 11, 1902, the companies all signed an agreement for the immediate delivery of their plants and property, without waiting for any appraisement theretofore stipulated for in each instance.

On August 12, 1902, the very day of the organization of the International Harvester Company with a total capital of $120,-000,000, Mr. Lane appeared before the board of directors and offered to sell the Milwaukee Harvester Company plant as a going concern, including its bills receivable and the plants of the McCormick Harvesting Machine Company, the Deering Harvester Company, the Plano Manufacturing Company, and the Warder, Bushnell & Glessner Company, and to furnish $60,-000,000 of working capital, to be represented by accounts and bills receivable of the McCormick Harvesting Machine Company, the Deering Harvester Company and the Plano Manufacturing Company, or in cash, for the $120,000,000 of the capital stock of the company, and on August 13, 1902, this proposition was accepted. The property turned in was of greater value than the stock issued for it. This case, therefore, involves no question of overcapitalization.

In pursuance of this agreement there was turned over to the company $40,000,000 of the bills receivable of the McCormick Harvesting Machine Company, the Deering Harvester Com-

pany, and the Plano Manufacturing Company, guaranteed by them, respectively. In all Mr. Lane did in this matter he was acting upon the suggestion of his counsel, Messrs. Guthrie, Cravath & Henderson. He was compensated, but there never was any idea upon his part that he owned any of the properties. He was a mere conduit or instrumentality in the transaction.

The International company shortly acquired all the stock of the Milwaukee Harvester Company, as it had already acquired the plant. It reduced the capital of the Milwaukee Harvester Company to $1,000,000, and changed the name to the International Harvester Company of America, hereafter called the America company. It was for a considerable time officered by the same men who held the offices in the International company. A contract was entered into between the International company and the America company by which the former contracted to sell to the latter its entire output and the latter undertook the responsibilities of reselling the same. The America company, in addition to buying the manufactured products of the International, bought from outside parties some threshers, wagons, plows, etc., and resold them; but the dealing in all property not the product of the International company only amounts to about 2½ per cent of its business. All the stock of the America company is still the property of the International company.

The two defendant railroads are switching roads to the factories of the International company; one acquired in the consolidation mentioned, and one constructed by the new company. The International Flax Twine Company, the Wisconsin Steel Company, and the Wisconsin Lumber Company are auxiliary companies of the International company, and the personal defendants are officers and directors of the last-named company.

It is alleged in the petition that these five companies produced over 85 per cent of all harvesting machinery sold in the United States, and it is admitted in the answer that the said companies produced approximately 80 to 85 per cent of the binders, mowers, reapers, and rakes.

In January following the consolidation of the five companies, the International company acquired the D. M. Osborne & Co.

stock, and the companies thus combined manufactured a still greater percentage of the harvesting machinery used in the United States and nearly the whole of that exported from the United States. The five companies except the Milwaukee company all took stock in the new company, and with the exception of the Warder, Bushnell & Glessner Company took stock for the entire amount of property turned over by them, and this amounted to $93,400,000 of the $120,000,000 capital of the new company. $6,600,000 of the capital of the new company was paid to J. P. Morgan & Co., of which $3,148,196.66 was for the Milwaukee Harvester Company's property and business, and $3,451,803.34 was for services and expenses in connection with the organization of the International company. Thus $1,000,000 of the capital of the new company was clearly covered, without any new or additional working capital. By agreement among all the parties who were to receive shares of stock in the International, all the stock except enough to qualify directors was vested in voting trustees, namely, George W. Perkins, Cyrus H. McCormick, president of the McCormick Harvesting Machine Company, and Charles Deering, of the Deering Harvester Company. These voting trustees were maintained for ten years.

The day of the transfer to the International Harvester Company of the five plants, Cyrus H. McCormick, Harold F. McCormick, Stanley McCormick, all of the McCormick Harvesting Machine Company, and Cyrus Bentley, the Chicago attorney of the company, Charles Deering, William Deering, James Deering, and Richard F. Howe, all of the Deering Harvester Company, and John J. Glessner, of the Warder, Bushnell & Glessner Company, and William H. Jones, of the Plano Manufacturing Company, were all chosen directors of the International Harvester Company and constituted the majority of the board.

When the D. M. Osborne & Co. purchase was made, while the International bought all the stock, it permitted the Osborne company to continue to appear to be independent. It is claimed that this was done to enable the Osborne to collect its bills receivable, which were not acquired by the International. There was commercial advantage in claiming not to be associated with

the International. Many persons were opposed to buying from it, and for two years the Osborne company persistently advertised that it was independent.

While under the old-time law of warranty it might be justifiable for the Osborne company to conceal its relations with the International, there can be no excuse for the affirmation upon its part that it was independent after it had been acquired by the International.

The seller may let the buyer cheat himself *ad libitum*, but must not actively assist him in cheating himself. 1 Parsons on Contracts (9th Ed.), page 615.

The International had bought all the stock of the Osborne company, and it had been transferred to a trustee for it, and there was, in the fact that the Osborne company might better collect its bills receivable, no basis to justify the International in making a contract under which the Osborne company could continue to advertise falsely that it was an independent concern, when it had in fact been merged with the International. It is safe to say that from January, 1903, the competition of the Osborne company was in name only and did not exist in fact.

What has been said of the Osborne purchase is true in principle of purchases made by the International of the Keystone company, the Minnie Harvester Company, and the Aultman-Miller plant.

Prior to the consolidation the first five companies were in fierce competition for trade, and especially was this true of the McCormick and the Deering companies, and this competition extended, not only to price, but to the granting of expert assistance and numerous free items with machines. The result of the combination was that all this competition at once wholly ceased, except within the limitation of agents' commissions.

The defendants claim that the objects of the organization were:

First, to build up the foreign trade;

Second, by the combination to secure more capital to enable them to continue the battle in the foreign market;

Third, by enlarging the scope of the business so as to include

other lines of agricultural implements to make an all-the-year-around business;

—and that it was not the intention to oppress the domestic market, and that they have not done so.

It does appear that since the combination the foreign trade has been greatly increased. This trade of all the combining companies was $10,400,000 in 1902, and has grown under the defendants' management to $50,000,000 in 1912. This vast growth is to the credit of the energy and enterprise of the defendants. But the growth of the trade of the companies who formed the combination was at the time of the consolidation very recent, and the trade was rapidly increasing just prior to the combination. With the knowledge that the foreign trade was making such a remarkable growth at the time of the consolidation, whether the separate companies would have increased their business as much as the defendants have done is a mere matter of speculation, on which we can venture no opinion.

It is claimed that the consolidation brought $60,000,000 of available cash to the new company with which to expand the foreign trade. This is not true. The government claims that not more than $10,000,000 of new cash was furnished, but in no event did it exceed $20,000,000. Forty million dollars of this so-called working capital was furnished in bills receivable of the old companies, just as available to the old companies as to the new; and $60,000,000 was issued for the tangible property of the old companies and the expenses of J. P. Morgan & Co. in connection with the organization of the new company, and for the Milwaukee company.

Soon the International began buying and constructing plants to extend its business from the prior one of the manufacture of harvesting machinery to the manufacture of all of the five classes of agricultural implements heretofore referred to. Consequently a distinction is drawn in argument between what are called the old lines and the new.

It is contended by the government that the International used its prior monopoly of the old lines to impose its new lines upon dealers and it includes this among numerous charges of oppression upon purchasers.

While the evidence shows some instances of attempted oppression of the American trade by the International and the American companies, such cases are sporadic, and in general their treatment of their smaller competitors has been fair and just, and if the International and American companies were not in themselves unlawful, there is nothing in the history of the expanding of the lines of manufacture, so as to make an all-the-year-around business, that could be condemned.

[1] The real question is whether the combination of the companies was illegal in the beginning, or became so with the additions subsequently made.

This court is clearly of the opinion that the process by which it was made to appear that the properties were sold to Lane was merely colorable.

[2] No weight is attached therefore to the means by which the combination was formed if a combination within the purview of the statute was created. That it was a combination of five companies is clear. The fact that this combination took the form of a new corporation is immaterial.

Was this combination in restraint of trade? It substantially suppressed all competition between the five companies, and the restraint of competition between combining companies is as illegal as destruction of competition between them without combining.

In *United States* v. *E. I. Du Pont De Nemours & Co.*, it is said:

> While all this is true, the recent decisions of the Supreme Court make it equally clear that a combination cannot escape the condemnation of the Anti-Trust Act merely by the form it assumes or by the dress it wears. It matters not whether the combination be "in the form of a trust or otherwise," whether it be in the form of a trade association or a corporation, if it arbitrarily uses its power to force weaker competitors out of business, or to coerce them into a sale to or union with the combination, it puts a restraint upon interstate commerce, and monopolizes or attempts to monopolize a part of that commerce, in a sense that violates the Anti-Trust Act.

In *United States* v. *American Tobacco Co.*, 221 U. S. 106, 179, 31 Sup. Ct. 632, 648 (55 L. Ed. 663), it is said:

> Applying the rule of reason to the construction of the statute, it was held in the Standard Oil Case that as the words "restraint of

trade" at common law and in the law of this country at the time of the adoption of the Anti-Trust Act only embraced acts or contracts or agreements or combinations which operated to the prejudice of the public interests by unduly restricting competition or unduly obstructing the due course of trade, or which, either because of their inherent nature or effect, or because of the evident purpose of the acts, etc., injuriously restrained trade, that the words as used in the statute were designed to have and did have but a like significance. It was therefore pointed out that the statute did not forbid or restrain the power to make normal and usual contracts to further trade by resorting to all normal methods, whether by agreement or otherwise, to accomplish such purpose. In other words, it was held, not that acts which the statute prohibited could be removed from the control of its prohibitions by a finding that they were reasonable, but that the duty to interpret, which inevitably arose from the general character of the term "restraint of trade" required that the words "restraint of trade" should be given a meaning which would not destroy the individual right to contract and render difficult, if not impossible, any movement of trade in the channels of interstate commerce — the free movement of which it was the purpose of the statute to protect. The soundness of the rule that the statute should receive a reasonable construction, after further mature deliberation, we see no reason to doubt. Indeed, the necessity for not departing in this case from the standard of the rule of reason which is universal in its application is so plainly required in order to give effect to the remedial purposes which the act under consideration contemplates, and to prevent that act from destroying all liberty of contract and all substantial right to trade, and thus causing the act to be at war with itself by annihilating the fundamental right of freedom to trade, which, on the very face of the act, it was enacted to preserve, is illustrated by the record before us. In truth, the plain demonstration which this record gives of the injury which would arise from and the promotion of the wrongs which the statute was intended to guard against, which would result from giving to the statute a narrow, unreasoning, and unheard of construction, as illustrated by the record before us, if possible, serves to strengthen our conviction as to the correctness of the rule of construction, the rule of reason, which was applied in the Standard Oil Case, the application of which rule to the statute we now, in the most unequivocal terms, re-express and reaffirm.

[3] Suppression of competition, where the parties to a combination control a large portion of the interstate or foreign com-

merce in the articles, and where there is no obligation to form the combination arising out of the fact that the parties to the same are losing money, or the like, has been held an undue restraint of trade.

[4] We think it may be laid down as a general rule that if companies could not make a legal contract as to prices or as to collateral services they could not legally unite, and as the companies named did in effect unite the sole question is as to whether they would have agreed on prices and what collateral services they could render, when their companies were all prosperous and they jointly controlled 80 to 85 per cent of the business in that line in the United States. We think they could not have made such an agreement.

If the five companies which formed the International had been small, and their combination had been essential to enable them to compete with large corporations in the same line, then their uniting would, in the light of reason, not have been in restraint of trade, but in the furtherance of it; but when they constituted the largest manufacturers of their articles in America, if not in the world, and held jointly about 80 to 85 per cent of the trade, and two at least of the companies forming the combination were prosperous, their combining was, when similarly viewed, an unreasonable restraint of trade. If the business of the separate companies combining was unsuccessful, it could be claimed that their combination was reasonable, in view of the rule of reason as proclaimed by the Supreme Court; but it is conceded that the McCormick and the Deering companies "had established reasonably successful and prosperous businesses," so that question is eliminated.

There is no limit under the American law to which a business may not independently grow, and even a combination of two or more businesses, if it does not unreasonably restrain trade, is not illegal; but it is the combination which unreasonably restrains trade that is illegal, and if the parties in controversy have 80 or 85 per cent of the American business, and by the combination of the companies all competition is eliminated between the constituent parts of the combination, then it is in restraint of trade within the meaning of the statute, under all of the decisions.

We conclude that the International Harvester Company was from the beginning in violation of the first and second sections of the Sherman Law, and that this condition was accentuated by the reorganization of the American company and by the subsequent acquisitions of competing plants, and that all the defendant subsidiary companies became from time to time parties to the illegal combination, and the defendant companies are combined to monopolize a part of the interstate and foreign trade. It will therefore be ordered that the entire combination and monopoly be dissolved, that the defendants have 90 days in which to report to the court a plan for the dissolution of the entire unlawful business into at least three substantially equal, separate, distinct, and independent corporations, with wholly separate owners and stockholders, or in the event this case is appealed, and this decree superseded, then within 90 days from the filing of the procedendo or mandate from the Supreme Court the defendants shall file such plan, and in case the defendants fail to file such plan within the time limit the court will entertain an application for the appointment of a receiver for all the properties of the corporate defendants, and jurisdiction is retained to make such additional decrees as may become necessary to secure the final winding up and dissolution of the combination and monopoly complained of, and as to costs.

Sanborn, Circuit Judge (*dissenting*).

It is the opinion of the majority of the court that the property and the foreign and interstate business of the International company must be divided into at least three substantially equal and independent parts, or placed in the hands of a receiver under a decree of this court, because in 1902 five companies theretofore engaged in the manufacture and sale of harvesting machinery, controlling about 85 per cent of the interstate and foreign trade therein, combined in the International company, ceased and have not since resumed competition among themselves. With profound respect for their judgment, I find myself forced to dissent from it: (1) Because it seems to me to give insufficient consideration to the trade conduct of the defendants at the time this suit was commenced in April, 1912, and for seven years before that date; (2) because

the crucial issue in this case is not whether or not in 1902 or 1903 the defendants or their predecessors, by reason of the suppression of competition between five or more companies, made a combination or an attempted monopoly in restraint of trade, but it is whether or not ten years afterwards, in 1912, when the complaint in this suit was filed, the International company and the other defendants were then unduly or unreasonably restraining or monopolizing interstate or foreign trade, or threatening so to do; and (3) because the evidence in this case has forced upon my mind the deep and abiding conviction that, for at least seven years before the commencement of this suit, the defendants had not been, and then were not, either so doing or threatening so to do.

1. Conceding, but not admitting, that if the combination of 1902 and 1903 had been challenged in 1903 or 1904, before the actual effect of the conduct of its business by the defendants upon interstate and foreign trade had been demonstrated by the actual trial of it from 1905 to 1912, a court might have presumed that the defendants were violating the Anti-Trust Law, and have so found on the theory that those who have power to violate a law are presumed to do so, yet the demonstration by actual trial, which the evidence seems to me to present, that at the time this suit was commenced the defendants were, and for at least seven years before that time had been, conducting the business of the International company and their business without unduly restraining or monopolizing interstate or foreign trade ought to, and in my opinion must, far outweigh that questionable presumption.

2. The controlling issue in this case is not what combination or monopoly was made in 1902, 1903, or 1904, nor whether or not that combination was violate of the Anti-Trust Law. It is: Were the defendants in 1912 doing or threatening to do acts which so unreasonably restrained or monopolized interstate or foreign trade that it is the duty of this court of equity to enjoin and prevent their future performance? If, therefore, a combination or monopoly, in unreasonable restraint of trade, was made in 1902, 1903, or 1904, the proceedings to punish for the making thereof were barred many years before this suit was commenced.

Section 4 of the act gives jurisdiction to this court "to prevent

and restrain violations of this act," but it grants this court no power to punish past violations thereof. This suit is not a proceeding to punish the defendants for deeds done in the past. It is a suit in equity under section 4 to prevent and restrain future violations of the Anti-Trust Law. It looks to the future, not to the past, and this court is not only without jurisdiction to punish defendants for past violations of this law, but persons who at some past time combined to unreasonably restrain or monopolize interstate or international trade were not thereby deprived of their right thereafter and now to conduct such trade in obedience to the law.

3. The particular facts proved in this individual case not only fail to show that the defendants were unduly or unreasonably restraining or attempting to monopolize interstate or foreign trade, or threatening so to do at the time this suit was commenced and for seven years before that time, but they establish the converse.

That the Anti-Trust Law is but the embodiment and application to interstate and foreign trade of the ancient English rule of public policy against undue and unreasonable restraints of trade and unreasonable monopolies, that it does not forbid all restraints upon such trade or all attempts to monopolize it, nor all restrictions of competition therein, but those only which are unreasonably injurious to the public, that the reason for and the purpose of the Anti-Trust Act are the same as the reason for and the purpose of that English rule of public policy, that the test and standard by which to determine whether or not the defendants in any case are unreasonably restraining or monopolizing interstate or foreign trade is the same which had been applied under the English rule of public policy for years before this Anti-Trust Act was enacted, and that, as Chief Justice White said, "the statute under this view evidenced the intent not to restrain the right to make and enforce contracts, whether resulting from combination or otherwise, which did not unduly restrain interstate or foreign commerce, but to protect that commerce from being restrained by methods, whether old or new, which would constitute an interference that is an undue restraint," are now rules of interpretation and application of this law conclusively established by the repeated decisions of the highest judicial tribunal in the land.

It is equally well established that the reason for the prohibition by the English rule of public policy and by the statute under consideration of unreasonable restraints of and attempts to monopolize trade was and is that, by unduly restricting competition, they are injurious to the public in that (1) they raise the prices to the consumers of the articles they affect, (2) limit their production, (3) deteriorate their quality, and (4) decrease the wages of the labor and the prices of the materials required to produce them. Undue injury in the ways just stated to the public (that is to say, to the consumers and makers of the articles produced or sold) is the basis and reason for the prohibition and the test of undue or unreasonable restraint or attempt to monopolize. And if in any individual case the weight of the evidence fails to prove that the defendants' conduct of their business is so restricting or threatening to restrict competition in the articles they make or sell as to unduly injure the public by (1) raising the prices of the articles to the consumers, or (2) limiting their production, or (3) deteriorating their quality, or (4) decreasing the prices paid for the labor or materials required to produce them, or (5) by unfair and oppressive treatment of competitors, neither undue nor unreasonable restraint of competition, nor of trade, nor undue attempt to monopolize is established. The reason for the rule and for the prohibition in the law does not exist, and the law is inapplicable. Such a case the evidence in this case seems to me to present.

Counsel for the government recognize the fact that it was essential to the grant of the relief they sought that they should plead and prove that, at the commencement of this suit, the defendants were committing, and threatening to commit, the acts constituting undue restriction of competition, undue restraint of trade, and undue attempt to monopolize trade which have been recited, and they alleged that they were committing them in their complaint. The main charge in their pleading was that the defendants between 1903 and April 30, 1912, had, by means of the International company, unduly restricted competition in the manufacture and sale of harvesting machinery, drawn to itself the business therein, excluded other manufacturers and dealers therefrom, and that they threatened to

continue so to do. The evidence, however, seems to me to have established the following facts, which in my judgment proved the contrary:

The amount of domestic sales of the old lines claimed to have been monopolized (that is to say, of the harvesting machinery) by the five companies whose business was acquired by the International company in 1902 was $46,142,158.64 in that year. The amount of the domestic sales of like machinery by the International company in 1903 was $37,763,858.55, a decrease of 18.16 per cent; in 1904 it was $32,337,917.32, a decrease in the two years of 29.92 per cent; in 1905 it was $30,999,632.59, a decrease in the three years of 32.82 per cent; and in 1912 it was only $39,062,455.36, which was 15.34 per cent less than the amount of the domestic sales of the combining companies in 1902.

The average yearly acreage and production of small grain in the United States during the ten years prior to 1913 was greater than during the nine years prior to 1903. But the yearly average domestic sales of the International company of all agricultural machinery, including both the old lines charged to have been monopolized and the new lines, such as harrows and cultivators, during the ten years prior to 1913, was $46,810,067, which was more than a million dollars less than the domestic sales of the vendor companies in 1902.

In 1903 the International company sold 98.15 per cent of the binders sold in the United States; in 1912 only 85.04 per cent thereof. In 1903 the International company sold 92.05 per cent of all the mowers sold in the United States; in 1912 only 72.98 per cent thereof. In 1903 the International company sold 84.91 per cent of the rakes sold in the United States; in 1911 it sold 67.79 per cent thereof.

The average number of binders sold in the United States yearly by the five combining companies during the five years prior to 1902 was 152,364; the average number sold yearly by the International company during the first ten years of its existence was 91,465.

In 1903 the International company had five competitors, who in that year sold in the United States 1960 binders, while in

1912 these competitors sold 15,631 binders and three new competitors sold 3979. In 1903 eight competitors of the International company sold in the United States 17,985 mowers, and in 1912 these and six other competitors sold 60,816. In 1903 ten competitors of the International company sold in the United States 27,753 rakes, and in 1911 these and five other competitors sold 42,723, while the International company sold 157,160 in 1903 and only 89,912 in 1912. In 1901 and 1902 in the section of Nebraska south of the Platte river, the combining companies sold substantially all the binders, but in 1912 the evidence tends to show that their competitors sold about one half the binders sold in that country.

During all of the ten years prior to 1913, the International company has had active and successful competitors in the manufacture and sale of harvesting machines, and during those years new competitors have established themselves in the business and become successful. Among its competitors in the manufacture and sale of harvesting machinery are the Acme company, which entered the field in 1907 or 1908, which makes harvesting machinery only, which conducts a growing and successful business, and which sold in the United States 11,000 harvesting machines in 1908 for $779,672 and 31,000 harvesting machines in 1912 for $2,100,000; Deering & Co. with an issued capital stock of over $50,000,000, which sold 490 mowers in 1906 and 7314 in 1911; the Johnston Harvester Company with an issued capital stock of $1,800,000 whose sales of binders increased from 1002 in 1903 to 3027 in 1911, whose sales of mowers increased from 2527 in 1903 to 7026 in 1911, whose sales of corn binders increased from 528 in 1903 to 3150 in 1911, and whose sales of rakes increased from 1855 in 1903 to 5200 in 1911; the Independent Harvester Company which entered the field with the manufacture of 954 mowers and 135 binders in 1910 and increased its output to about 2700 mowers and about 1900 binders in 1912; the Wood Mowing & Reaping Company and several others, while the J. I. Case Threshing Machine Company, with an issued capital stock of $20,000,000, was constructing, when this suit was commenced, a large plant to manufacture a binder to be sold in competition with those of the International

company. The foregoing facts portray the course of the business in the old lines. In the new lines scores of companies and tens of millions of dollars and capital were and are engaged in active and successful competition with the International Harvester Company. The facts which have been recited, and other facts and circumstances to the same effect, seem to me to establish the conclusion that, during the ten years of the operation of the International Harvester Company, neither it nor the defendants were, nor are they, drawing to it its competitors' share of the interstate trade in harvesting machinery, or excluding them therefrom, and that, on the other hand, the International company's proportion of this trade has been decreasing and that of its competitors increasing.

Counsel for the government charged that the defendants bought factories and failed to operate them in order to restrain and monopolize the trade, but the proof was that they operated every factory they purchased. And the purchase of factories and the organization and operation of subsidiary companies to produce or prepare the raw materials needed for the manufacture of their machines, or to manufacture new lines of implements, was a just and lawful method of conducting their business and tended not to restrain but to promote trade and competition.

If competition is desirable, the entry of a new competitor into any line of manufacture or trade is ordinarily lawful and must be generally beneficial.

The government charged that the defendants systematically bought up patents on and inventions of harvesting machinery in order to make or perpetuate a monopoly in the trade in it. But the proof was that the defendants have no patents upon any parts of any of their harvesting machines, and that any manufacturer is free to make and sell any or all parts of them in competition with them.

Counsel for the government alleged that the defendants reduced the prices of its machines in certain localities in order to drive competitors out of the trade, and increased their prices in other localities to make up the loss, and that it committed many oppressive and unjust acts to restrict competition and monopolize

trade. Volumes of evidence were taken regarding these averments. The conduct of the business of the defendants for years in all parts of the land were searched and proved. Among the innumerable acts of the defendants and their agents in conducting their vast business for a decade, the government found some that were unfair to competitors, but they were either unauthorized acts of subordinate agents or sporadic and exceptional instances. The weight of the evidence of the officers and agents of their competitors who came in large numbers to testify, and of all the witnesses upon the subject, is so overwhelming that the general conduct and the almost universal practice of the defendants and their agents was and is free from all methods and acts either unlawful, unfair, or oppressive towards their competitors, that it has left no doubt that the consistent and persistent purpose, policy, rule of action, and practice of the defendants has been and is to avoid and prevent all acts and methods unfair, unjust, or oppressive towards their competitors, to leave competition with them free, to give to them full and fair opportunities to secure shares of the trade and business in which they are all engaged, and to carry on their own trade honestly, justly, and fairly.

During the ten years from 1902 to 1912 there was a general and substantial rise in the prices of machinery and commodities of nearly all kinds in the United States. Harvesting machines were improved and made more durable and efficient. But their prices to the consumers remained nearly stationary, and increased far less than the prices of other agricultural machinery the trade in which was not claimed to have been restrained or monopolized. The chief harvesting machine was the binder. Its price advanced about 5 per cent during some of the intermediate years, but was substantially the same in 1912 for a better machine than it was for a poorer machine in 1902, while the prices of cultivators, wagons, and plow goods, which were certainly not monopolized, advanced from 10 to 30 per cent.

The government charged that the defendants monopolized the trade in binder twine and increased its price to the consumers, but the proof was that in 1912 the inmates of two state's prisons and fourteen other competitors were selling binder

twine; that one of them, the Plymouth Cordage Company, sold 100,000,000 pounds of it in that year, while the International company sold only 112,000,000 pounds in the United States and 22,000,000 pounds in Canada; and that the price of binder twine decreased from 11 cents a pound in 1902 to $7\frac{1}{4}$ cents a pound in 1912. Meanwhile the cost of the raw material required to make harvesting machines advanced, and the wages of the labor required to construct them increased from 20 to 30 per cent.

So it is that the evidence has convinced me that at least for seven years before this suit was commenced, and at that time, the defendants were neither unduly restricting competition in the manufacture or sale of the machinery and articles in which they were dealing or drawing to themselves an undue share of the business therein, or excluding other manufacturers and dealers therefrom, or practicing acts unjust and unfair to, or oppressive of, their competitors, or threatening so to do; that they were not injuring the public by raising the prices to the consumers of the articles in which they dealt, or limiting the production thereof, or deteriorating their quality, or decreasing the wages of the laborers employed to make them, or the prices paid for the materials required to construct them, or threatening so to do; but that they were doing the opposite of these things. And the acts of the defendants and the proved effect of their acts during at least seven years before this suit was commenced, to my mind, demonstrate the fact that they were neither unduly nor unreasonably restraining or attempting to monopolize interstate or foreign trade in the articles they made and sold, and that they and their case fall far without the prohibition of the Anti-Trust Law and the reason for it.

4. The only reason for the prevention or restraint of acts of defendants in a suit under the fourth section of the statute is, as we have seen, that they are or threaten to be unduly injurious to the public. If they are not thus injurious, or if they are beneficial, and such restraint or prevention of their acts would be injurious to the public, they should not be restrained or prevented. The defendants claim that the main purpose of the combination of 1902 and 1903 was to develop the foreign trade in American harvesting machines; that that development could

not be successfully made without a much larger capital than any of the combining companies possessed; and that the cessation of competition among the combining companies was merely incidental to the acquisition of the capital requisite to accomplish that purpose. The facts in this case are so clear that the purpose and intent of the defendants are not material. The prevention or restriction of their acts by the decree of a court of equity is always a matter within the sound judicial discretion of the chancellor or chancellors composing the court, and, while in exercising this discretion the rules of law and the facts already stated seem to me to be decisive, the following are not altogether unworthy of consideration. The proof is that during the ten years preceding 1913 the International company at great expense taught the people of foreign countries the use of American harvesting machinery, and developed the foreign trade therein in such a way that, while in 1902 the sales in foreign trade of machines, repairs, and twine by the companies whose business was acquired by the International company amounted to about $10,400,000, the sales of the International company in the foreign trade gradually increased until in 1912 they amounted to $50,896,000, and so that, while in 1903 the domestic sales of that company were 76.5 per cent, and its sales in the foreign trade were 23.5 per cent, of its total sales, in 1912 its domestic sales were 55.7 per cent, and its sales in the foreign trade 44.3 per cent, of its total sales. The employment of the necessary American laborers and salesmen at the increasing wages the defendants have paid and are paying to make and to sell in other lands these machines and the purchase at the increasing prices paid of the materials to construct this vast volume of machinery unavoidably tends to increase the wages of the laborers and the prices of the materials, and hence to benefit the public, and any receivership or subdivision of the property and the business of these defendants cannot fail to tend to cripple and diminish this business, to restrain the advance, or to decrease the wages of the laborers and the prices of the materials required to carry it on, and thereby to inflict injury upon the public.

Again, the combination denounced and the International company, in which it was embodied, have been in existence,

and that company and the other defendants had been conducting their business, for almost ten years before this suit was commenced. If the making of that combination was originally a violation of the Anti-Trust Act, the prosecution of the defendants at law under sections 1 and 2 of the Anti-Trust Act for that violation was barred many years before this suit was commenced.

5. The evidence in this suit seems to me to present a new case under the Anti-Trust Law. No case has been found in the books, and none has come under my observation, in which the absence of all the evils against which that law was directed at the time the suit was brought, and for seven years before, was so conclusively proved as in this suit, the absence of unfair or oppressive treatment of competitors, of unjust or oppressive methods of competition, the absence of the drawing of an undue share of the business away from competitors and to the defendants, the absence of the raising of prices of the articles affected to their consumers, the absence of the limiting of the product, the absence of the deterioration of the quality, the absence of the decrease of the wages of the laborers and of the prices of the materials, the absence, in short, of all the elements of undue injury to the public and undue restraint of trade, together with the presence of free competition which increased the share of the competitors in the interstate trade and decreased the share of the defendants. Neither the Standard Oil company case, nor the American Tobacco company case, nor any other authority cited, seems to me to rule this case, because in none of them was there such affirmative and, to my mind, conclusive evidence that for years before the suits were commenced the defendants had practiced no acts and pursued no methods which constituted an undue restraint of trade or an unreasonable attempt to monopolize it.

And because in this suit this court is without power to punish past violations of the Anti-Trust Law, and the limit of its jurisdiction is to prevent and enjoin future acts violative thereof, because the making of the combination of 1902 and 1903, whether violative of the Anti-Trust Law or not, did not deprive the defendants of their right thereafter and now to conduct their business in obedience to that law, because the question in this case is not whether or not the combination of 1902 and 1903

was violative of that law, but it is whether or not in April, 1912, when this suit was commenced, the defendants were unduly or unreasonably restraining or attempting to monopolize interstate or foreign trade, because it was not the effect of the Anti-Trust Law, nor was it the intent of the Congress which passed it, to prohibit all restriction of competition or all restraints of interstate or foreign trade, or all attempts to monopolize parts of it, but only those restraints and attempts to monopolize which are unduly injurious to the public by (1) raising the prices to the consumers of the articles they affect, (2) limiting their production, (3) deteriorating their quality, (4) decreasing the wages of the laborers and the prices of the materials required to produce them, or (5) practicing unfair and oppressive treatment of competitors, because the evidence has convinced me that for at least seven years before this suit was commenced, and at that time, the defendants were not injuring the public by unduly or unreasonably restricting competition in the manufacture or sale of the machinery or articles which they were making and selling, or by drawing to themselves an undue share of the business therein, or by excluding other manufacturers or dealers therefrom, or by practicing acts unjust or unfair to, or oppressive of, their competitors, that they were not injuring the public by raising the prices to the consumers of the articles they made or sold, or limiting their production, or deteriorating their quality, or decreasing the wages of the laborers employed to make them, or the prices paid for the materials required to construct them, that they were not threatening to do these things, but they were doing the opposite of these things to the substantial benefit of their competitors, of the consumers of their products, of the laborers who make them, the men who furnish the material for them, and the public in general, because the acts of the defendants during these seven years do not constitute that undue or unreasonable restraint of or attempt to monopolize interstate or foreign trade forbidden by the Anti-Trust Act, and because, in my opinion, the prevention or restraint of these acts or this business of the defendants, or the splitting of their business and property into three or more independent parts, or the seizure of it by a receiver, by virtue of a decree of a court of equity, would

not tend to prevent undue restraint of, or undue attempts to monopolize, interstate or foreign trade, but, on the other hand, would tend to produce or foster the very evils at which the Anti-Trust Act was leveled, to wit, the restriction or lessening of competition, the increase of the prices of the machinery and articles affected, the deterioration of their quality, the limitation or reduction of the product and the diminution of the wages of the laborers making them and of the prices of the materials required to produce them to the substantial injury of the public, I am unable to concur in the opinion or the decree against the defendants in this case. In my opinion, a decree should be rendered that the complaint in this suit be dismissed without prejudice to the right of the United States to bring another suit of like character against any of the defendants whenever any of them is found to be engaged in the commission of any acts in violation of the anti-trust statute.

THE KEYSTONE WATCH CASE[1]

Unfair Practice

As might be expected in a record so voluminous, the evidence, whether oral or in writing, is not always either relevant or competent; but we shall not discuss it in detail, contenting ourselves with finding such of the ultimate facts as seem to be necessary.

The present Keystone company is the second of that name, both of them being Pennsylvania corporations. The first was organized in 1886, and was the successor of several Philadelphia manufacturers, beginning with James Boss, the inventor of the filled or rolled-plate case, and comprising also John Stukert, Hagstoz & Thorpe, and C. N. Thorpe & Co. These firms and their corporate successor manufactured superior cases and acquired an excellent reputation in the trade. Owing to the death of certain persons that had been interested in the business, and to the consequent need of providing for the demands of their estates, some new financial arrangements seemed to be desir-

[1] *U. S.* v. *Keystone Watch Case Co.*, Circuit Court, 218 Fed. Rep. 502; decided Jan. 2, 1915.

able. At the same time an association known as the T. Zurbrugg Co. was manufacturing an inferior grade of watch cases at Riverside, N.J., and some of the persons interested in that association had certain financial connections with the two estates just referred to. (A year or two before, the Zurbrugg company had bought a small business, owned by J. Muhr & Brother, of Philadelphia, and had combined it with their own.) It was believed by the old Keystone company and by the Zurbrugg company that a union of the two enterprises would be mutually advantageous, so that both grades of cases might be made under one management. Accordingly, a new company — the present defendant — was incorporated, and this company bought outright the title to the plant, business, and good will, of the old corporation and of the Zurbrugg company. The persons interested in these two enterprises received either cash or stock in the new company at their option. This transaction took place in July, 1899.

In the following August the Philadelphia Watch Case Company was organized for the purpose of selling the product of the Riverside plant. All of its capital stock was owned by the Keystone company. As already stated, this product was inferior in grade, and a separate sale thereof seemed advisable in order to avoid confusing the cases made in the two plants respectively.

Early in 1900 the capital stock of the New York Standard Watch Company, a New Jersey corporation with a plant at Jersey City, was in the market. This company did not manufacture cases, its only product being inexpensive movements. The Keystone company purchased for cash the capital stock of the Standard company, the object being to supply the demand for cheap completed watches. The Keystone company had found some difficulty in selling its cheaper watch cases because of the lack of cheap movements to go with them, the movements manufactured by the principal movement companies being relatively too expensive. The separate corporate organization of the Standard company was continued, and the size and the product of the plant were increased.

Early in January, 1901, the Philadelphia firm of Bates & Bacon, a small manufacturer of cases, sold all its property to

the Keystone company, the machinery at cost, and the finished product at selling prices.

In the same month, a small movement business at Waltham, Mass., owned by the United States Watch Company, offered to sell out to the Keystone company, and in June, or thereabouts, the sale was made. The object of the purchaser was to manufacture medium-priced movements at Waltham, and for this purpose additional capital was furnished, and the plant and facilities were enlarged. A New Jersey corporation by the same name — United States Watch Company — with an authorized capital of one million ($1,000,000) dollars was organized, and operated the Waltham plant for about two years, manufacturing medium-priced movements only. The business, however, was not successful.

In January, 1903, the watch-movement business of the E. Howard Clock Company was offered for sale by a receiver. This company had formerly manufactured an excellent and favorably known movement, but for several years the business had been discontinued. Seeing an opportunity to use the reputation of the Howard movement to aid the United States Watch Company's business at Waltham, the Keystone company bought the good will, machinery, and trade-marks, of the Clock company, so far as they related to watches and watch movements, and moved everything to Waltham. The United States Watch Company was thereupon abandoned, and a new company was organized under the laws of New Jersey, called the E. Howard Watch Company — all of its stock being owned by the Keystone company — and the Howard company took over the United States company's plant, and has since been manufacturing fine and expensive movements at Waltham. The watch movements formerly manufactured by the E. Howard Clock Company had in no way competed with the product of the Keystone company, whose movements were neither high grade nor expensive.

In December, 1902, the common stock (4000 shares) of the Crescent Watch Case Company, of Newark, N.J., was offered to the Keystone company, and was purchased in the following February, being paid for partly in cash and equivalent

obligations, and partly ($\frac{1}{4}$) in the common stock of the Keystone company. (Later, in 1906, the preferred stock of the Crescent was also bought by the Keystone company for cash.) The reasons for the purchase were these: the Crescent cases and the movements of the well-known Waltham Watch Company (not the United States company referred to above) had both been handled by one firm, who acted as the exclusive selling agent for each, so that the sale of Keystone cases to be used with the movements of the Waltham Watch Company was interfered with; and the sale of Crescent cases to be used with other than Waltham movements was also interfered with. The union of the two companies seemed likely to eliminate both these hindrances. Moreover, their respective sales were in different markets, where they competed, not so much with each other as with other manufacturers, of whom there were several actively engaged in business and apparently prospering. The union was voluntary on the part of both companies; the Keystone company exercised no pressure or coercion upon the Crescent, and the trade of neither was restricted or diminished. Moreover, prices to the public were not raised as the result of the union, except perhaps to a small extent.

From time to time the issued capital stock of the Keystone company had been increased, reaching $6,000,000 in the end—all of it having been issued for cash—and in 1910 all the assets of the Philadelphia, the Standard, the Howard, and the Crescent companies were formally transferred to the Keystone company, and the four companies first named abandoned their separate organizations (which had theretofore been maintained) and ceased to exist, either actually or in effect.

In 1903, the Keystone company became interested in the watch-case business in Canada under the following circumstances:

For several years the American Watch Case Company, of Toronto, Limited, had been manufacturing in the Dominion, but its plant was not satisfactory, and for this or some other reason its business was for sale. This fact became known to the Keystone company, and to the Elgin and the Waltham movement companies. No one of these three had been able to do much in the Canadian market, owing in part to the tariff of

that country, and in part to other reasons not important to enumerate. These three companies determined, therefore, to use the Toronto company in order to enter the Canadian market with Keystone cases, and also with Elgin and with Waltham movements, and to that end bought the capital stock of the Toronto company — the Keystone acquiring 851 shares out of 2000, and the rest being held largely in the interest of the Elgin and the Waltham companies. The American Watch Case Company has since that time improved its methods of manufacture, and has increased its business. Later, a selling agent for Canada was organized, in which the Keystone company owns the capital stock. If this transaction has any relevancy, we need only add that it did not restrain, but rather benefited, the foreign trade with Canada in cases and in movements.

Up to this time, we discover nothing unlawful in the operations of the Keystone company. No doubt it had been growing, and it had grown in part by acquiring or controlling several other plants, but it had not acquired them by improper methods, and it had not used its acquisitions improperly. There was no concealment about its growth, and the trade was well informed about its operations. Its plants were enlarged or improved, the volume of production was increased, prices were not inflated, competitors were not unlawfully attacked, and we find nothing in the evidence that would justify us in condemning the foregoing steps in the company's activity. A merchant may without offense add one department to another as his business prospers, or his ambition expands; for the size and the varied character of his enterprise do not in themselves violate the Anti-Trust Act. Size does not of itself restrain trade or injure the public; on the contrary, it may increase trade and may benefit the consumer; but, if the power given by the volume of a particular business is improperly used to injure either a competitor or the public, or if such power evidently tends toward the injury of either, the mischief either done or threatened is condemned by the statute.

In this connection, it may be observed, that as power increases the temptation to abuse it is likely also to increase, so that the acts of an influential factor in a particular trade may well be scrutinized with more suspicion than the acts of a weak and in-

conspicuous contributor. And we have now reached a point in these transactions when we think the evidence establishes that the defendant company did use its power unlawfully. Beginning in 1904 or thereabouts, it made several attempts — perhaps not very numerous, but numerous enough — that showed a definite purpose to restrain trade by attempting to fix and maintain prices, and by using a species of boycott or blacklisting in order to lessen the trade of its rivals. We shall not stop to detail the attempts of this character that were made during the period from 1904 to 1910, because the policy and system to which we refer were manifested with unmistakable distinctness in the latter year, and were carried on with vigor and persistence. It will be sufficient, therefore, to state what was attempted, and what was actually done, from January, 1910, forward.

On the 15th of that month the following circular was formally adopted by the Keystone company's board of directors, and was sent to 131 of the largest and most prominent jobbers or wholesalers in the United States:

THE KEYSTONE WATCH CASE COMPANY
Nineteenth and Brown Sts.

PHILADELPHIA, January 15th, 1910.

DEAR SIR:

We enclose herewith our new price list which we are mailing to the retail trade to-day. These prices are subject to the usual catalogue discount and the case discount only.

We also enclose memoranda of the prices at which Boss, Crescent, Planet, Crown, and Silveroid cases, and Excelsior watches will be billed in future to our jobbers. These prices are net, subject to the cash discount only.

These prices are confidential.

For the best interests of our business we have determined to sell our goods exclusively to jobbers whom we find voluntarily conforming to our wishes as to the disposition by them of such goods.

We shall make all specific sales, except of Howard watches, without any restrictions whatever.

Whether or not our wishes as hereinafter stated be complied with, we shall from time to time exercise our right to select the jobbers to whom we shall sell our goods, and we shall, irrespective of any past dealings, refuse to sell to those jobbers who, in our opinion, handle our

goods in a manner detrimental to our interests or whose dealings with us are in any other respect unsatisfactory.

Our present wishes are as follows:

First. Our goods bearing the following trade-marks, to wit, Boss, Crescent, Planet, Crown, Silveroid, and Excelsior, will be sold by us to our jobbers at fixed prices subject to a cash discount, and we desire that sales of these goods by jobbers, whether to retailers or to jobbers, shall be without deviation at the prices fixed by us for sales to retailers subject only to the cash discount.

Second. Howard watches are sold only under the terms of the license covering their sales.

Third. On all our other goods we place no restrictions as to the prices at which they are to be sold by jobbers.

Fourth. And further, we desire that the jobbers to whom we sell our goods bearing the following trade-marks, to wit, Howard, Boss, Crescent, Planet, Crown, Silveroid, and Excelsior, shall not deal in any watch-cases other than those manufactured by us.

Fifth. All advertisements of our goods will be subject to our approval.

Very truly yours,

THE KEYSTONE WATCH CASE COMPANY

Officers or agents of the company followed up this circular by visits to the selected jobbers — although perhaps not to all of them — and assured them that the letter meant exactly what it said, and that the policy outlined therein would be rigorously carried out. And it was insisted upon and was carried out. Some of the jobbers assented to the company's wishes, and with more or less reluctance gave up buying from other manufacturers, while the jobbers that refused to assent were cut off from the Keystone product altogether, unless they obtained it through surreptitious channels.

We do not think it necessary to spend time over the foregoing circular. We regard it, not as a request but as a threat; and not as an empty threat, but as a real menace from a strong manufacturer. The defendant company attempts to justify both the circular and its own conduct before and after the circular was issued, by the argument that the selected jobbers were its "exclusive agents," and therefore were properly burdened with any conditions to which they might agree. But the relation of principal

and agent did not exist between the company and the jobbers. They were not agents, paid for their services by salary or commission, and owing a duty to report and account; they were merely customers of the defendant company, who bought its unpatented cases by a transaction of outright purchase, and thereby took a complete title to the cases and acquired an unrestricted right to sell. And, moreover, it should be observed that they were already established customers, not only of the defendant company, but also of its competitors, and had already become trade outlets for every manufacturer of cases whose wares they had been accustomed to buy. Now, what the defendant company did was either to close these already existing and already utilized outlets, or to narrow them materially, so far as the cases of its competitors were concerned; and we think the proposition need not be discussed, that this was *pro tanto* a direct and unlawful restraint of trade.

And it is not sufficient to answer, that these competitors appear to have withstood the attack with more or less success, and that their total trade did not always, or even often, diminish. Where or how they made up the loss that they must have sustained, is not material; it is certain that they must have lost whatever trade they had previously enjoyed with those jobbers that yielded to the threat of the defendant's circular; and it seems clear, therefore, that in this degree at least there was an unlawful restraint of trade. In other words, if this section of the trade had not been taken away from the defendant's competitors, we may reasonably suppose that they would have retained it; and this fact seems to be a final answer to much of the evidence, the tables and lists of varying scope and value, that have been laid before us, and were offered to show that on the whole not much damage, if any, was done by the offending circular and the defendant's unlawful conduct. A recent decision of the Supreme Court on the general subject of blacklisting is *Eastern States &c. Ass'n* v. *United States*, opinion delivered June 22, 1914.

The proportion of the trade in filled cases that the defendant company was enjoying from 1903 onward is in dispute, and is not altogether easy to determine with accuracy; but we shall do the defendant no injustice if we adopt the figures of its counsel

and say, that "When the acquisitions were completed (the company) had from 50 to 55 per cent; when the petition was filed, it had from 42 to 47 per cent." But we have no hesitation in adding, that even with this proportion of the business the defendant did not dominate the trade. It had then, and has always had, a number of active and successful rivals, and we see no reason to doubt that there was business enough for all. No complaint on the part of the other manufacturers would have been made or would have been justified, as far as we can determine, if the defendant had not undertaken the policy we have condemned; and it is essentially this — and one other matter to be spoken of presently — that furnishes the government with just ground for complaint. It is probable that the policy has not been successful, save in a limited degree and for a limited time; but in our opinion it is a plain restraint of trade within the Act of 1890, and the government is entitled to enjoin it.

One or two other matters referred to in the pleadings and in the evidence should be briefly referred to: First, the defendant company's agreements with the Waltham and the Elgin movement companies respectively. These companies are not parties to the bill, and no relief is prayed against the agreements. The subject was introduced by the government merely as an argument to support its averment that the defendant has been steadily pursuing the definite object of restraining interstate and foreign trade in filled cases. The facts are as follows:

The course of the watch trade in the United States differs from its course in foreign countries. Here, both the jobber and the retailer buy movements and cases separately, and the retailer fits the case and the movement together as the ultimate consumer may desire. But in foreign countries both the jobber and the retailer deal in the completed watch. Efforts by the American companies to change the foreign course of trade were unsuccessful, and it was found that the custom there must be respected, and that watches must be exported in completed form. The agreements referred to were made with the object of securing a share in this comparatively unoccupied field. The Keystone company obtained from the Waltham and the Elgin companies the exclusive right to sell their movements in certain foreign

countries, fitting the movements into the Keystone cases. The Waltham contract covers the continent of Europe, with the exception of France and Spain, and in this territory the Waltham company had previously been doing but little business. The Keystone cases were to be made at the Riverside plant, and all the movements were sold to the Keystone company at favorable prices, for such export trade only. The Elgin contract makes the Keystone company the sole export jobber of the Elgin movements except for trade to Canada, and fixes prices of the movements for export only, providing that the Keystone company shall fit the movements into its own cases, and shall then export the complete watch.

We see nothing unlawful in these contracts. On the contrary, they appear to show a laudable effort to increase American trade with foreign countries. They were intended to help our own merchants in the struggle to enter new markets, and we are unable to find that they operated injuriously to restrain the trade of any American competitor.

The other subject is the system under which the Howard watch was sold. The defendant company attempted to restrict the prices at which the wholesaler or jobber might sell to the retailer, and to this end made a direct agreement with the jobber. As we understand the decisions such an agreement was within the company's lawful rights. Certain material parts of the Howard watch were covered by *bona fide* patents taken out and used for a lawful purpose, and as the owner of these patents the company had the right to make a direct agreement with the jobbers whereby a minimum price was fixed at which the jobber might sell. *Bemet* v. *Harrow Co.*, 186 U. S. 70; *Henry* v. *Dick Co.*, 224 U. S. 1. But the company went further, and by mere notice to the retailer, accompanying the box in which the watch was sold by the jobber, attempted to fix the minimum price at which the retailer might sell to the consumer. No direct agreement was made with the retailer. When the company sold the watch to the jobber, it had fully exercised its right to vend, and had no right to use the notice subsequently given in order to control the price at which the retailer might sell. *Bauer* v. *O'Donnell*, 229 U. S. 1.

We should end the discussion at this point, if it were not for the recent decision in *U. S.* v. *Harvester Company*. [Reprinted herein at p. 634, *supra*.] The majority opinion, as we understand it, is put upon the ground, that the combination there in question — which was made in 1902, but was not proceeded against until 1912 — was and continued to be unlawful because at the beginning it suppressed competition between corporations that controlled about 80 per cent of the trade in harvesting machines. This conclusion was reached, although there was no evidence of coercion in the original combination, and no evidence of oppression or of actual injury to trade in the subsequent conduct of the business. In the principal opinion, Judge Smith says:

> While the evidence shows some instances of attempted oppression of the American trade by the International and the American companies, such cases are sporadic, and in general their treatment of their smaller competitors has been fair and just; and, if the International and America companies were not in themselves unlawful, there is nothing in the history of the expanding of the lines of manufacture so as to make an all the year around business that could be condemned.
>
> The real question is, whether the combination of the companies was unlawful in the beginning, or became so with the additions subsequently made.

And Judge Hook in his concurring opinion takes the same ground, saying:

> The International Harvester Company is not the result of the normal growth of the fair enterprise of an individual, a partnership, or a corporation. On the contrary it was created by combining five great competing companies which controlled more than 80 % of the trade in necessary farm implements, and it still maintains a substantial dominance. That is the controlling fact; all else is detail. . . .
>
> It is but just, however, to say and to make it plain that in the main the business conduct of the company toward its competitors and the public has been honorable, clean, and fair. Some petty dishonesties were tracked in at the start, mostly by subordinates who had been in the service of the old company, but they were soon gotten rid of. In this connection it should also be said that specific charges of misconduct were made in the government's petition which found no

warrant whatever in the proof. They were of such a character and there was so much of them, apparently without foundation, that the case is exceptional in that particular.

Judge Sanborn dissented, on the ground that as the suit was in equity the court had no power to punish past violations of the Anti-Trust Act, but was only authorized to prevent and enjoin further acts violative thereof; taking the position that the question for decision was, whether at the beginning of the suit in 1912 the Harvester company was unreasonably restraining, or attempting to restrain or monopolize, interstate or foreign trade. In considering this question he laid stress upon the argument that the statute forbids such acts only as injure the public unduly in some of the following particulars:

(1) raising the prices to the consumer of the articles they affect;
(2) limiting their production;
(3) deteriorating their quality;
(4) decreasing the wages of the laborers, and the prices of the materials required to produce them; or
(5) practicing unfair or oppressive treatment of competitors.

After reviewing the evidence he came to the conclusion on the facts, that for at least seven years before the suit was begun the defendant had not been injuring the public either by unreasonably restricting competition, or by acquiring an undue share of the business, or by excluding other manufacturers or dealers, or by practices that were unjust or unfair or oppressive to competitors, or by raising prices to the consumer, or by limiting production of the articles manufactured, or by deteriorating the quality of such articles, or by decreasing the wages of labor, or by reducing prices of raw materials; and that the defendant was not threatening to do these things in the future. On the contrary he found that the acts complained of by the government had had the opposite effect, and had resulted in benefit to competitors, to consumers, to laborers, and to the producers of raw materials.

With this difference of opinion in a strong and highly respected court, it may perhaps have some value if (with some

hesitation) we add our own contribution to the discussion of this vastly important and much considered subject. We shall try to state our views briefly, although it may conduce to clearness if we outline the subject from the beginning. The Act of 1890 is directed against restraint of interstate or foreign trade; that is, against restraining the business of buying or selling for gain, whenever the transaction forms a part of commerce among the states or with foreign countries. Trade may be restrained — that is, hindered, or obstructed, or destroyed — in many ways and by many devices, but these are all covered by the first and second sections of the Act. In these sections two classes or prohibited acts are described; (1) the concerted action of two or more persons, which may take the form of a contract, a combination in whatever form, or a conspiracy; and (2) monopoly, or the attempt to monopolize, which may be the act of one person alone, or of more than one. These two classes are intended to be all-embracing, and thus far in the history of the statute no variety of device has escaped their sweep.

In the usual meaning of the word monopoly may be said to be the acquisition of something for one's self, and perhaps it would be applied most appropriately when the whole of a given trade is acquired. Practically, however, we need not contemplate so extreme a case of control or acquisition, and indeed the Act itself is not primarily concerned with an offense so rare. The second section deals with the monopolizing, or the attempt at monopolizing, "any part" of the trade or commerce referred to; and it is clear enough therefore that Congress had chiefly in mind, not so much the monopoly of a whole (although the language might properly be construed to cover that also), as the much more likely case of the monopoly of a part smaller than the whole. But the question immediately arises — at what point does a business become so large that the statute condemns it? Or — to state the question in other words — is the mere size of a business enough to bring it within the disapproval of the Act? Section 2 gives us no help, for "any" part if strictly construed might range from a minute and inconsiderable fraction, to a part just less than the whole. If therefore a merchant, either an individual or a corporation, by the most commendable zeal

and industry should succeed in diverting to himself a very small part of a competitor's business, he would be monopolizing a "part" of the trade, and would be condemned by the letter of the Act. And in like manner, if the statute is using the strict meaning of "restraint of trade," no merchant could act in combination with his own partner in successful competition for part of a rival's business, even by the fairest and most honorable means, except at the risk of "restraining" trade. Further examples are needless; many more might be given. Clearly, therefore, as it seems to us, the Act could not have been intended to bear a meaning so subversive; and it seems plain that the supreme court was abundantly justified in turning to the rule of reason, and in holding that of necessity Congress must have been dealing with undue or unreasonable restraints of trade, whether such restraints take the form of monopolies in whole or in part, or of concerted action under any guise whatever.

But to say that a transaction is undue or unreasonable implies that it has been judged by a standard. The standard of course is reason, but various questions at once present themselves for answer. For example, who is to apply the standard? The legislation of Congress does not attempt the task itself, and under our system of government the duty must of necessity be undertaken by the courts, who must judge each case according to its own facts. But when such a question comes to be considered, where is a court to find the standard of reason? It seems to us that it must be found in the gradually accumulated results of general experience and observation, in the gathered wisdom of the community, for this is the product of a common and a prolonged effort by men who theorize and by practical men alike to deal as fairly, as justly, and as equitably, as may be possible with situations that are often obscure and complicated, and of high importance to large classes and to many individuals. Obviously a standard should have a true relation to the subject measured; and, since the inquiry here is, whether in a given case trade is likely to be, or has actually been, unduly restrained, reason can answer the question only by going to the facts of life and drawing upon the accumulated store of knowledge.

Now, the world has already learned some lessons that have

become part of its common stock. One of them is, that, when men announce their intention in entering upon a given transaction, declaring it to be the accomplishment of a particular object, their declaration may usually be accepted as correct. Not always, of course, but as a rule; and especially is this true, if the concealment of their intention would advance their interest. Let us suppose that several persons combine to do certain acts that may, or may not, have the effect of restraining trade. If they expressly declare their intention to be the restraint of trade, we shall hardly go wrong in believing them. And if such a situation is unlikely, a better illustration may be found in supposing that they agree to do the acts, but say nothing about their intention. In that event, if according to the common course of experience and observation the acts proposed will certainly have the result of restraining trade, their unexpressed intention will be of no consequence whatever; neither will it be of any consequence, if the reasonable probability be that trade will be restrained by the proposed conduct.

But another and ordinarily a better way of determining whether a course of conduct under examination is in restraint of trade is sometimes available, and that is, by considering its actual effect. It goes without saying that such a test can only be applied after the course in question has actually been carried out in some degree, has actually been tried by experience; and this leads to the further question — When should the standard of reasonableness be applied? Evidently this will depend on the time when the question is submitted for decision. This time may either precede the proposed course of conduct, or it may follow the beginning of such a course so quickly that no body of experience, or no sufficient body, has yet come into existence. In that event, the nature of things compels the court to enter the field of prophecy, or of probable anticipation. In such a situation, nothing else can be done. A court can only deal with the situations that are laid before it, and in the case supposed it must avail itself of whatever light may be had, and must exercise its best judgment with such aid as may be at hand. But, if the suit be deferred until the lapse of time and the actual effect of the conduct complained of have permitted

facts to accumulate and have tried the project in question by the test of experience, we can hardly doubt that prophecy or probable anticipation should be considered inferior in force to the evidence of what has actually taken place. In this world we must do our best with the means at our disposal. Even if prophets are always in danger of being discredited by the event, we are sometimes compelled to speculate about the future; and our duty then is to check our speculations as much as possible by taking account of such probabilities as may arise from past experience and observation. In like manner, when we are face to face with what has actually happened, we may safely lay prophecy aside, in order to accept the services of a better guide, one that can be relied upon with a firmer confidence.

And this brings us to the next question, no matter at what point of time the inquiry may be undertaken; namely, what are the ordinary marks of such a course of conduct as may properly be condemned as a restraint of trade? Without attempting to enumerate them exhaustively, a few general observations may be made. Trade is restrained by putting hindrances in the way of the persons that conduct it. Whatever makes it more difficult for such persons to carry on their business, restrains them, and restrains their trade; but (to speak generally) as every successful effort of a merchant to increase his own trade makes it harder for his rivals to succeed and therefore restrains their trade; and as Congress certainly did not intend to condemn the proper exercise of business zeal and energy, we must recur to the rule of reason and ask — not merely what is restraint of trade, but what is unreasonable restraint of trade? On this subject we are certainly able to say some things with confidence. Competitors must not be oppressed or coerced; fraudulent or unfair or oppressive rivalry must not be pursued. And if these words are criticized as too general, we may reply that such generality is apparently unavoidable as some recent legislation of Congress testifies, and moreover we may safely deny that the words are too vague for satisfactory use; for it must be remembered, that the common agreement of moral opinion in the community furnishes an adequate guide to their practical meaning and their practical application. They are not likely to be mis-

apprehended or misapplied. Then, too, prices must not be arbitrarily fixed or maintained. Ordinarily the play of the great forces that influence the market will determine prices, and these forces must be allowed to have their unhindered effect. And a corollary from this consideration is that an artificial scarcity must not be produced, since the effect of such a scarcity is to raise prices to the consumer. Moreover, the public is also injured if quality be impaired so that the old price buys a worse article; and other injuries are done, if the wages of the laborer be arbitrarily reduced, and if the price of raw material be artificially depressed.

In the complexity of human affairs there may be other methods of unreasonably restraining trade, and these may be left for consideration as they are made to appear; but those already referred to are the methods that have usually been employed, and we need not enter the field of conjecture. Now, if all or some of these marks of unlawful restraint be present or may fairly be expected, the statute requires the application of an appropriate remedy; but, if none of them be present after sufficient experience has shown what will actually happen, on what satisfactory ground is condemnation to be pronounced? Not, we think, merely on the ground of size. As population has swelled, and as vast aggregations of men have multiplied their wants, the inevitable trend of modern affairs has called for large business enterprises as well as for small; and we think it no more than reasonable to say that when a large business has proved itself to be beneficial and not harmful to the community it should not be condemned merely because it is large. We do not consider, and we do not deny, the right of a nation to adopt such a legislative policy in this respect as its constitution may permit; but, until a policy of limitation be so adopted, we see no possible test of reasonableness to be applied except such tests (and those like them) as have already been sufficiently referred to. And, from whichever side the subject may be approached — from the side of what is likely to happen, or from the side of actual experience — the standard of reasonableness should be applied according to the facts and circumstances of the particular case under examination.

As will no doubt be observed, we have already applied the rules we have been considering to the case in hand, and have expressed our opinion concerning the several acts of the defendant company that are attacked by the government, so that we need say nothing further except a word concerning the relief that should be granted. The defendant declares that the policy of boycott had been given up before the bill was filed — and there is some testimony to this effect — but the circular has never been withdrawn or negatived, and the company's resolution of January, 1910, has never been rescinded. We feel no hesitation in acting on the assumption that the policy was at least formally in force when the government began the suit now before us, and we have no doubt that an injunction should be granted. But we see no sufficient evidence that the public interest requires us to break up the existing corporate entity: *U. S.* v. *Great Lakes Towing Company*, 208 Fed. 746. The record satisfies us that the watch case business is not suffering from the absence of live and healthy competition, and except in the directions already mentioned — namely, the retail sales of the Howard watch, and the policy of boycott — we think the court is not called upon to interfere. But, in case conditions in the future should make it desirable for the government to ask for additional relief, even to the point of breaking up the defendant corporation, we shall retain jurisdiction of the bill, with leave to the government to take such action hereafter as may seem appropriate.

THE NATIONAL CASH REGISTER CASE[1]

The proceedings against this substantial monopoly are significant because of their persistence; because of their nature, being criminal rather than civil; and because they disclose so clearly the oppressive tactics once prevalent which were not then regarded even as bad form in business. Yet they so far shocked even the Harrison Administration, that an indictment was returned in 1893 against Patterson, then President. But the case was allowed by the Attorney General to lapse, "because of reconciliation of complaining witness with defendants." The lion having swallowed the lamb, in fact, professed

[1] *Patterson et al.* v. *U. S.*, 222 Fed. Rep. 599; rendered March 13, 1915. Omissions are not indicated in the text.

contentment with its included state. So little at that time was an offense against one regarded as an injury to all! These later proceedings were instituted, civilly in 1911 and criminally a year later, against Patterson and twenty-nine other employees of the company. The trial resulted in a verdict of guilty as to 29 out of 30 of the defendants. Fines aggregating $135,000 were assessed and jail sentences up to a year for Patterson were imposed. The opinion herewith passes upon the exceptions taken and the technical irregularities of the first trial. It was affirmed by the Supreme Court in June, 1915. The highly technical portions which deal with flaws in the indictment and defects in procedure are omitted, as of little interest either to the economist, the moralist or the citizen at large. Nor should the mere fact that the statute of limitations permits the defendants to go scot free close our eyes to the enormity of the offenses against public decency which were committed. Not even the avowedly high standards of efficiency and fair dealing which now obtain, can obscure the fact that the National Cash Register Company was for many years an industrial pirate. — ED.

This is a criminal prosecution under Act July 2, 1890, 26 Stat. 209, c. 647. The indictment was found February 22, 1912, and contains three counts. The offense which the first charges is that of engaging in a conspiracy in restraint of interstate trade and commerce under the first section of the act, and that which each of the other two charges is monopolizing a part of such trade and commerce under the second section. The defendants were 30 in number. Each, for many years, had been connected with the National Cash Register Company, a corporation engaged in the business of manufacturing and selling cash registers, with its principal place of business at Dayton, Ohio, within the district of the lower court, in the capacity of an officer or agent. All but four were so connected when the indictment was found; those four ceased their connection, three in 1910 and one in 1911; and four of them had been connected for at least 20 years continuously prior to its finding. The conspiracy with which they were charged was directed against competitors of that company, and the monopolizing was the exclusion of its competitors from such trade and commerce for its benefit. Trial was had, and all the defendants save one were found guilty under each count. Motion for new trial was sustained as to one, and the indictment was nollied as to him. Sentence as to another was deferred because of sickness, and pronounced as to other 27, who are the plaintiffs in error herein. The sentence of one, John H. Patterson, president, was a fine of $5000 and confinement in jail for one year; that of 23, such confinement for one year; and that of three for nine months.

The first count is quite long; each of the other two is short. The first makes certain introductory statements before charging the offense and alleging the facts, the doing of which it claimed constituted its commission. Those statements are: [Omitted.]

These introductory statements were followed by a charge of the offense in general terms.

From this charge in "generic terms" the count descended to "particulars." The eleven things by means of which the defendants conspired to accomplish those objects may thus be summarized:

(1) Inducing, hiring, and bribing employés of the competitors of the National Cash Register Company, named, to disclose to it the secrets of their business, particularly as to prospective buyers, customers who had ordered, customers who had not fully paid, shipments to customers, agents, and dealers, volume of business, places where done, inventions, financial conditions, and connections.

(2) Inducing, hiring, and bribing employés of carters, truckmen, express companies, railroad companies, and telephone and telegraph companies to disclose to it the secrets of their employers pertaining to the carriage and transportation of the cash registers of such competitors.

(3) Instructing and requiring all its sales agents to ascertain and report all facts and details pertaining to the business of such competitors, and particularly of competitors coming into the competitive field.

(4) Using its influence and that of its agents with, and the making of unwarranted and false statements to, banking and other institutions, to injure the credit of such competitors and prevent them from securing accommodation of money, credit, and supplies.

(5) First. Instructing and requiring all its sales agents to interfere with, obstruct, and prevent, in every way possible, sales of such competitive cash registers by such competitors, and their agents and dealers in cash registers, and by any and all means to bring about sales of its cash registers, and the displacement of such competitive cash registers, and the substitution of its genuine cash registers therefor in the hands of users of cash registers, and particularly (*a*) by making to prospective purchasers of such competitive cash registers false statements derogatory of same, and reflecting injuriously upon the business character and financial credit of such competitors, and their ability and intention to perform their undertakings and make good their warranties and promises, and offering to sell to them cash registers at prices much less than the regular and standard prices and on unusually favorable terms as to payment; (*b*) by inducing persons who have already ordered such competitive cash registers to cancel

their orders and purchase its cash registers through such statements and offers; (*c*) by inducing purchasers of such competitive cash registers who had only partially paid therefor to repudiate their contracts of purchase through such statements and offers and allowing them the amount they had paid; (*d*) by inducing purchasers of such registers, whether they had paid in full or not, to surrender them to it, in exchange for its registers for the purpose of exhibiting them in the windows of its stores where its registers were on sale, bearing placards with the word "Junk" or "For Sale at Thirty Cents on the Dollar" printed thereon; (*e*) by offering, to prospective purchasers of such registers, registers in similitude of any competitive registers they were contemplating buying, at a price much lower than the regular price thereof, and in cases at much less than the manufacturer's costs, which registers so offered were manufactured by it solely as a so-called "knocker," so as to cause such purchasers to believe that it was of such cheap and poor construction that it was a waste of money to purchase it or such registers; (*f*) and by offering to prospective purchasers of such registers such knockers with weak and defective mechanism, and claiming that the registers they were contemplating buying had the same weak and defective mechanism. Second. And instructing and requiring its sales agents secretly to weaken and injure the interior mechanism, and remove and destroy parts of such mechanism of the cash registers of such competitors in actual use by purchasers, and thereby to cause them to become dissatisfied and substitute for them its cash registers.

(6) Making by it to such competitors and to purchasers and prospective purchasers of their cash registers of threats to begin suits in the courts against them for infringing and having infringed its patent rights pertaining to its cash registers, when, as each of them well knew, no such patent rights existed, and no such suit was contemplated or would really be begun, and such threats were made merely to harass such competitors, purchasers, and prospective purchasers, and deter such competitors from manufacturing and selling such competitive cash registers in such interstate trade and commerce and such prospective purchasers from buying and using such competitive cash registers.

(7) Beginning, in other cases, by it against such competitors and against purchasers of such competitive cash registers of suits for infringement of its patent rights pertaining to its cash registers, when, in those cases, they each well knew no patents upon which such suits could be maintained were in existence or owned or controlled by it, and when, as they each well knew, none of those suits would be

further pressed, but all such suits would be kept pending only as long as they served the purpose of harassing such competitors and purchasers.

(8) Organizing cash register manufacturing concerns and cash register sales concerns and maintaining them, ostensibly as competitors of their company, but in fact as convenient instruments for use in gaining the confidence and obtaining the business secrets of competitors and accomplishing the objects of the conspiracy and making such use of competitive concerns from time to time acquired by it.

(9) Inducing by offers of much greater compensation the agents and servants of such competitors and dealers patronizing them to leave their employment and cease patronizing them and to enter its employment and patronize it.

(10) Applying and causing application to be made for patents upon the cash registers and the improvements thereupon of such competitors, for the purpose of harassing them by interference proceedings and suits and threats to institute such proceedings.

(11) Using of or originating and using of and instructing and requiring of its agents and sales agents to use of or to originate and use such other unfair means excluding other concerns besides it from engaging in said interstate trade as might at any time become or appear to them or those agents or sales agents to be necessary or convenient to accomplish the object of the conspiracy, a description of which means other than already described the grand jury are unable to set forth, because such means were so numerous in kind and shifting in character as to make such description impossible.

We think it clear that there was substantial evidence to the effect that there was a conspiracy on the part of those officers and agents of the National company who then had to do with competition against most, if not all, of the competitors named who were in existence before the American of Columbus came into existence, which was not later than the early part of 1907, except the Peninsular, Burdick-Corbin, and Dial, as long as they were in existence within the twenty-year period, and that this conspiracy included the use of some, if not all, of the means specified, and other means not specified aimed to be covered by the eleventh item, and that when that company came into existence there was a generic conspiracy against all competitors, at least all who might endanger the National's supremacy, which generic

conspiracy had been in existence at least from the beginning of the twenty years. In an issue of a publication of the company seemingly for distribution amongst its officers and agents, of date May 1, 1892, occur these statements:

> If the opposition knew what is in store for them, they would not waste any more time and money staying in the business. They are all beginning to realize that there is no hope for them.
>
> It is only a question of whether we propose to spend the money to keep down opposition. If we continue, it is absolutely certain no opposition company can stand against this company and its agents. If necessary, we will spend five times as much money as we have already done, in order to down opposition. If they really believe this, they will throw up the sponge and quit.
>
> We are receiving overtures to buy out opposition. We will not buy them out. We do not buy out; we knock out.

In an issue August 1, 1895, occurs this statement: "We are determined to absolutely control the cash register business."

And in an issue of date March 25, 1897, after setting forth the policy of the company of frankly informing a competitor of the purpose to drive him out of business, occurs this statement:

> This, it is true, is what is called "securing a monopoly"; but we think there can be no possible economic or other objection to it. Cash registers are not a necessity of life. Any one who chooses can do business without them, thus contributing nothing to the "monopoly."

It is then stated that "this monopoly" "is managed upon a liberal and broad-minded plan." And at a convention of the district managers held at Dayton, July 22, 1907, the defendant John H. Patterson, president, thus expressed himself to them:

> We want Mr. Anderson of the competition department to give you a little idea of how we are going to control competition. We want Mr. Hayward also to give you a little talk. We want Mr. Muzzy to tell you how we are going to absolutely control the competition of the world, because we want you to feel this way. The first thing we aim to do is to keep down competition.

And again:

I asked the Standard Oil Company what was the secret of their success, and they said this question could be answered in a very few words. Men, nothing but men; men well organized; they will keep down competition and make things succeed.

In the publications of the company and in the communications between the officers and agents having to do with competition, terms of warfare were not infrequently used, such as battle, fight, enemy, ammunition, shot, whipped, victory, and flags flying. During that time all the competitors named then in existence retired from the field. The American of Philadelphia, Boston, Hallwood, International, Hubinger & Carroll, and Latimer quit. The National does not seem to have been the cause of the Latimer quitting. The Century, Chicago, Cuckoo, Globe, Ideal, Kruse, Lamson, Metropolitan, Navy, Osborn, Standard, Simplex, Sun, Toledo, Union, and Weller sold out to the National, and it discontinued their business. The American of Philadelphia and Boston quit because of infringement suits brought against them by the National, in which it was successful. The decisions in its favor against them are [citations omitted]. The result of this litigation may possibly have had something to do with other competitors quitting or selling out. Infringement suits were brought against most, if not all, the others, and these suits had more or less to do with their quitting or selling out. There was evidence tending to show in some of these instances at least that the claim of infringement was unfounded and known to be so, and that the suits for infringement were not brought in good faith, but for the sole purpose of aiding in driving the competitors from the field. The government claims that such was the case in all instances. In most, if not all, of these instances, some, if not all, of the other means were resorted to, and it is not unlikely that in some instances at least they were more effective than the suits. And such means were resorted to in some, if not all, the cases where the suits were successful. The Hallwood, International, Century, Chicago, Cuckoo, Globe, Ideal, Metropolitan, Navy, Osborn, Simplex, Sun, Toledo, Union, and Western retired from the field during the seven years prior to 1907. Most, if not all, of

the others retired before then, and mainly in the early part of the twenty-year period.

In justice to the National company and the defendants it should be noted that it was the pioneer in the cash register business and developed it. It owned the basic patents and must have acquired in a proper manner a very great number of improvement patents. In addition to this, it had the advantage of very great capacity in the management of its affairs. These two considerations together, without reference to any unfair treatment of its competitors, are sufficient in themselves to account in a large measure for the success it has attained. And it is not unlikely that its trade was pirated by other competitors besides the American of Philadelphia and the Boston, against whom it obtained decrees of infringement, and that these, as well as others, in their competition with it, resorted to some of the tactics complained of here.

We think it clear, also, that there was substantial evidence to the effect that this generic conspiracy was directed against the American of Columbus when it came into existence, and became specific as to it, and that it continued up until just shortly before the beginning of the three-year period. The only other competitors then in existence were the Peninsular, Burdick-Corbin, and Dial, neither of which, as stated, was of much consequence. That company was the successor of the International, and it in turn of the Hallwood. The Hallwood during its existence, which covered a number of years, was one of the National's most stubborn competitors. It went into the hands of a receiver in 1903 or 1904. There was evidence tending to show that an effort was made, whilst its assets were in such hands, by the National, to acquire them without its being known in the transaction. The International acquired them, and then the American. Its connection with the Hallwood not unlikely aided it in getting established in business soon after entering the field. So identified with the Hallwood was it that its machines were frequently called Hallwood, and it, sometimes, the Hallwood company. In view of its connection with the Hallwood company, one would expect the generic conspiracy to be directed against it as soon as it came into existence, and

so the government's evidence tended to show. May 4, 1907, the district manager at Detroit, Henry F. James, wrote to the assistant head of the competition department, Joseph E. Warren, that the Hallwood (*i.e.* American) situation in Detroit looked rather serious, and suggested the employment of the plaintiff in error Alexander W. Sinclair, then off the roll, to hire the Hallwood agent at that point. Warren answered that the competition did not warrant placing Sinclair on the roll again, and suggested that he (James) was in a better position to hire the agent than Sinclair. There was no evidence of anything else of a specific character during this year. But there were general statements as to competition which could not have had reference to any one but the American. Such was the statement of plaintiff in error John H. Patterson, at the convention of district managers July 22, 1907. June 20, 1907, the general manager, Hugh Chalmers, wrote to all the sales agents and salesmen, suggesting that they call on the users of competing machines and point out to them the weaknesses and deficiencies thereof, so that, even if they could not make a trade, they would cease to be a "plugger" for the opposition. And September 6, 1907, the head of the competition department, C. D. Anderson, wrote James at Detroit that the company was never in better shape to take care of competition than at that time, and for that reason they did not intend to let it increase again.

March 1, 1908, the plaintiff in error Sinclair entered the employ of the American and located at Detroit. It is possible that he was then still off the National's roll. He continued in its employ there until September 24, 1908. During this time a vigorous effort was made to drive him from the field, and it finally succeeded, when he reëntered the National's employ as a company salesman, and so continued until the trial. The plaintiffs in error Pflum, then general manager, Harned, then executive secretary, and Watson, then sales manager, participated in this effort. The method of attack was to prevent him from making sales of American machines and to displace such as he made. The way in which the former was attempted was by offering Hallwoods owned by the National at low prices — *i.e.* thirty cents on the dollar — in competition. The intention was to

construct a machine specially for that purpose. In a letter from James to Harned of date March 16, 1908, he stated that he needed a proper tool with which to fight Sinclair's competition, and requested that ten or twelve Hallwoods be sent him, "as our machine parallel to Hallwood will not be ready for some time," and Harned in his answer said that work on drawer-operated machine — which was the character of the American — was being pushed and they would be able to give it to him sooner than he had stated. But whether this machine was used in this connection does not appear. The way in which the displacements were brought about was by offering the regular National machines on unusual terms. Both methods were unfair. Their purpose was to drive Sinclair and the American which he represented off the field, so that the National might have it to itself. May 16, 1908, Harned wrote James, congratulating him on displacing six Hallwoods taken in part pay for six Nationals, and stated that all at the factory, including plaintiff in error Deeds, were pleased and gratified at the outcome, and that he had put a crimp in Sinclair from which he would have difficulty in recovery. June 9, 1908, James wrote Pflum that since Sinclair had taken hold he had blocked twenty-five of his sales and displaced nine. September 4, 1908, plaintiff in error Watson issued a circular to the selling force empowering them to sell Hallwoods at thirty cents on the dollar. There was evidence of unfair means being used during this same time at Los Angeles to prevent the sale of the American machine, the details of which need not be given. And September 10, 1908, James, in whose territory Grand Rapids, Mich., was located, wrote plaintiff in error Watson, wanting to know the conclusion of himself and plaintiff in error Pflum as to the situation at that place, and whether they had succeeded in hiring Cleaves, the agent of the American, and saying that, if they could not hire him, they should have some special men — *i.e.* company salesmen — there until they ran him out of business.

After Sinclair returned to the service of the National, he was sent to Toledo, Ohio, where he remained at least until in November, 1908. Whilst there he adopted the same tactics that had been used against him in Detroit to drive out the

agents of the American at that point. Finally, in the middle of January, 1909, James, the district manager at Detroit, left the service of the National, and in breach of a contract that he had with it at once entered the employ of the American and was placed in charge of several states, with headquarters at Detroit. In the early part of February, 1909, certainly not as late as the 22d of that month, the new district manager appointed to take the place of James at Detroit was installed. At a meeting of the sales agents and salesmen who were to be under him, held on that occasion, the plaintiff in error Watson was present and undertook to outline the policy of the National in meeting competition, and in the course of his remarks, according to one witness, he said that it would be necessary to use every means possible to put James out of business, and according to another that they did not want him to get a foothold in Detroit, and that they would move their executive offices to Detroit, but that they would put him out of business.

Thus it is that the government's evidence tended to establish a conspiracy on the part of some of the defendants at least against the American, and brought it down almost to the door of the three-year period. It remains to consider whether there was substantial evidence to the effect that it entered that door. Possibly in view of the fact that the American was still actively in business — that what had transpired preceding the three years down almost to it indicated an absolute and fixed purpose to restrain the trade of the American, if not to drive it out of business, without any indication of a change of purpose before the three years — and that the American was represented at Detroit by the National's former representative, against whom it had a grievance, it was for the jury, without more, to determine whether the conspiracy continued into the three years. But the case does not depend upon presumptions. Things were done within the three years by representatives of the National in restraint of the American's trade and commerce. According to the defendants, all that was done was by sales agents and salesmen, and none of the plaintiffs in error were directly connected with it; and what was done by sales agents and salesmen was scanty, in view of the fact that the National had seven hundred

fifty of such representatives distributed throughout the country, and the American was doing business all over it. They urge that what the government's evidence established was done should be taken as being all that was done. The American knew of all unfriendly action towards it, and actively assisted it in the prosecution of the case, and the evidence disclosed that it made a very thorough investigation. Here, according to defendants, was all that was done. In twenty-two instances sales agents and salesmen of the National attempted to induce purchasers of American machines, who had not paid for them, to repudiate their contracts by seller's talk and offering to allow them what they had paid on the purchase price of Nationals, in two, and possibly three, of which instances the attempt was successful. They occurred in fourteen different states and seventeen different localities. Ten of them occurred in 1909, seven in 1910, and five in 1911. Defendants would have it that these were all such instances, but the tendency of the testimony of Steubenrauch is to establish eight others, six of which were in 1910 and two in 1912, in Connecticut. In addition to these the acts in restraint covered by the government's evidence were the display in March, 1909, by the National's sales agents at Los Angeles, in California, in his show window, smashed-up Hallwood cash registers with a card bearing this inscription:

Hundreds of merchants have exchanged unsatisfactory Hallwood cash registers for Nationals. We sell them at 30 cents on the dollar. But as they have no commercial value and do not sell, we are compelled to break them up to make room and will sell as Old Junk.

—an unsuccessful attempt by the sales agent of the National at Dallas, Tex., in the winter of 1909–1910 to bribe a drayman in the employ of the American agent to tell him where he delivered every American machine, and an unsuccessful attempt by the sales agent of the National at Los Angeles, Cal., May 1, 1910, to induce the American agent at that point to leave its employ and enter that of the National. The defendants contend that it is more reasonable to account for these acts by a desire on the part of the sales agents and salesmen to make commissions than the existence of the conspiracy charged Un-

doubtedly these acts are small in number compared with the number which might have been, and it is possible to account for them on the grounds suggested. And the fact that James, the most important witness for the government, did not definitely testify to any specific acts in restraint of his trade after he became connected with the American is favorable to the defendant's position. But even on the basis that the foregoing list exhausts all acts in restraint of the trade and commerce of the American within the three years, and that these are to be accounted for, as defendants would have it, or as mere *sequelæ* of a conspiracy that terminated before the beginning of the three years, still we are constrained to hold that it was for the jury to determine whether the conspiracy continued into the three years. We have shown that the government's evidence tends to establish the continuance of the conspiracy almost up to the very beginning of the three years. Something happened shortly after the beginning of the three years calculated to terminate the conspiracy, which may account for nothing being done by the defendants in error within the three years indicating the continued existence of the conspiracy, and which, if it was the cause of its termination, involves its continuance into the three years. That was action on the part of James to call the National to account for its attitude towards and action against the American. On July 14, 1909, an information in the nature of a *quo warranto* on behalf of the people on relation of James was filed in the Supreme Court of Michigan against the National company to oust it from that state for violating its anti-trust laws, which proceeding resulted in a judgment for a fine on July 14, 1914. In the nature of things, some time must have been taken to prepare for the proceeding, and the evidence disclosed that James caused affidavits to be taken of unfair acts toward the American by National agents as far back as in March, 1909. It is not unlikely that the National became aware of this contemplated proceeding, and knowledge of it was calculated to cause it to take steps to end all action against the American which could reasonably be complained of. And we find that on April 1, 1909, the plaintiff in error Pflum sent the following letter to all the district managers, to wit:

THE NATIONAL CASH REGISTER COMPANY

New York, April, 1909

To All District Managers:

Mr. M. N. Jacobs: In the various conventions I have attended, I found that some of the newer members in the districts are not thoroughly clear on the best way to handle sales made by other companies. Please see that every agent in your district thoroughly understands our position in the matter.

You know what this policy is, but in brief will say that in no case will we permit any of our agents to misrepresent cash registers manufactured by other companies, neither will we permit any agent or person in our employ to induce any purchaser of a cash register made by any other company to break his contract and return the register to the manufacturer. With the line of registers that our agents now have, they are able to show the superiority of Nationals over those of any other make and at lower prices.

There has been no violation of our policies that I know of, but I give you this information because of the inquiries received from the newer men in the field.

Please see that these instructions are carried out in every detail and that the new men are so instructed on entering the field.

Yours very truly, WM. PFLUM,

W. P.—T. *Vice President and Manager*

There is room to claim that such is the only reasonable ground to account for this letter being written and sent out. If so, there is room to claim, further, that the conspiracy continued at least until then.

But we would not be understood as holding that, apart from this construction, the acts in restraint of the American's trade within the three years above given were not sufficient, in connection with the evidence tending to trace the existence of the conspiracy up to the beginning of the three years, to require that the question as to its continuance within the three years be submitted to the jury. The question is not whether those acts were sufficient to establish the entering into a conspiracy in the first instance, but the continuance of a conspiracy theretofore formed. And that list cannot be said to be exhaustive. We have heretofore noted that James in his letter to Harned of March 16, 1908, and Harned in his answer, referred to a drawer-

operated machine parallel to the Hallwood (*i.e.* American), which the National was making for the purpose of fighting the American therewith. The government's evidence tended to show that a machine known as 1000-line machine, and which not unlikely was this machine, was used only for the purpose of fighting the American and keeping it from making sales within the three years. If so, this could hardly be without some of the defendants being connected with it. The government's position here was combated strongly by the defendants, but we cannot weigh its evidence on this point as against that of the government. For these reasons, therefore, we think the case was for the jury, and the court did not err in overruling all the motions. It is not the province of an appellate court to weigh the evidence. What the trial court might do on a motion for new trial as to some of the defendants, in the view which we have taken of the nature of the offense charged, we need not pause to consider.

It is now in order to take up the assignments questioning rulings upon the admissibility of evidence. They are very numerous, but the consideration of them can be shortened by classification. In considering them, the case for the jury, as we have determined it to have been, should be kept constantly in mind. That case is whether within the three years the defendants conspired in restraint of the trade of the American of Columbus, by the use of the fifth and ninth means. No evidence that was not relevant thereto was admissible, and all that was was admissible, if not otherwise objectionable. The primary classification of these rulings is into those involving evidence that was admitted and those where the evidence was excluded. We consider first those where the evidence was admitted. In this connection it may be said generally that the admissible evidence was not confined to that which bore directly upon the existence of such conspiracy within the three years. All that was not otherwise objectionable tending to show the existence of a generic conspiracy when that company came into existence and its fixed and absolute character was relevant and admissible. Likewise as to all evidence tending to show that upon its coming into existence the generic conspiracy was

directed against it specifically and continued down to the beginning of the three years.

The admitted evidence involved in the rulings covered by the assignments relates to transactions within the three years and to transactions prior thereto as far back as the beginning of the twenty years. Here we consider first that which relates to transactions within the three years. And that may be divided into the evidence of the acts in restraint of the American trade, heretofore referred to, evidence of an act against that company, not heretofore referred to, and evidence of acts against the Michigan and Dial companies.

All of the evidence of acts against the American, heretofore referred to, was objected to, and the rulings admitting it are assigned as error. It is urged that none of those acts come within the means specified in the indictment, and that the eleventh item is insufficient, under the authority of the case of *United States* v. *Greene* (D. C.), 115 Fed. 343, 346. We think, however, that they fairly come within the fifth and ninth. Greater stress is made on the consideration that it was not shown that any of the defendants were connected with any of those acts. It is true that there was no direct evidence of such connection, apart from the use of the 1000-line machines; but this circumstance did not render evidence of those acts inadmissible. The government would base its admissibility on the doctrine of *respondeat superior.* It cites the cases of *United States* v. *Gooding*, 12 Wheat. 460, 6 L. Ed. 693, *Cliquot's Champagne*, 3 Wall. 114, 18 L. Ed. 116, and *Stockwell* v. *United States*, 13 Wall. 531, 20 L. Ed. 491, where it was held that:

> Whatever is done by an agent in reference to the business in which he is at the time employed and within the scope of this authority is said or done by the principal, and may be proved as well in a criminal as in a civil case in all respects as if the principal were the actor.

But this doctrine can have no application here, as the persons who did the acts — *i.e.* sales agents and salesmen — were not the agents of the defendants. They were the agents of the National company. They were under defendants, but this did not

make them defendants' agents. It urges further that they were co-conspirators with defendants, and under the case of *Clune* v. *United States*, 159 U. S. 590, 16 Sup. Ct. 125, 40 L. Ed. 269, what one conspirator does is evidence against the other, even though he is not a defendant or charged with being a party to the conspiracy in the indictment. Possibly this is sufficient to uphold the action of the court in admitting the evidence. But it is not necessary to rely on it. All the acts were done in the regular course of the business of the National company. Those sales agents and salesmen were under the direct supervision of some, at least, of the defendants. There was substantial evidence that prior to the three years the defendants were in a conspiracy to restrain the trade and commerce of the American of Columbus by causing such acts to be done, and the sole question was whether that conspiracy had continued into the three years. The doing of those acts was relevant to that issue. It was not an unreasonable inference that they were to be accounted for by the continued existence of the conspiracy. Possibly they are to be accounted for by the initiative of the sales agents and salesmen in their anxiety to make commissions or as mere *sequelæ*. But it was for the jury to determine how they were to be accounted for as between those three possible ways of doing so. The defendants contend that is a case of an inference upon or from an inference, and that this is not allowable under the cases of *United States* v. *Ross*, 92 U. S. 281, 23 L. Ed. 707, and *Manning* v. *Insurance Co.*, 100 U. S. 693, 25 L. Ed. 761. That it is a case of an inference upon or from an inference is attempted to be made out by tracing the course of inference in this way. An inference is first drawn that the sales agents and salesmen acted upon the instructions of the National company, and then the further inference is drawn that defendants were connected with such instructions. This case does not involve any such question. It is a case of immediate inference. The course of inference is not as claimed, but from the acts done to the conspiracy as the cause thereof. The court, therefore, did not err in admitting the evidence.

The evidence of an act against the company not heretofore referred to was as to something that happened in connection

with one of the attempts on the part of the National's sales agents and salesmen to induce purchasers of American machines to repudiate their contracts of purchase, to wit, the attempt as to Conrad Green & Sons of Portland, Ore., in the latter part of 1910. The agent of the American, who made that sale, left its employ the latter part of March, 1911, and entered that of the National. Evidence was admitted that after the delivery of the machine it was noticed to be out of order. The American agent made repeated attempts to fix it, but it remained out of order until he quit its employ. After he left, his successor, a repairman, who with the agent had examined the machine before its delivery and found it to be in perfect condition, examined it again and found that it was out of order because a piece of its mechanism was bent. The government's position was that the American agent had bent it, at the National's instance. There was no other evidence that the National had any other connection with the matter than that the American agent entered its employ four or five months afterwards and one of its competition men was seen in his store about three weeks before he did so. We do not think the evidence was sufficient to connect any National agent with the defective condition of the machine. There was no evidence of any other such act having ever been committed or attempted against the American. We, therefore, hold that there was error here.

The acts against the Michigan and Dial, evidence of which was admitted, were these. A salesman of the National attempted to induce a dealer in Michigan cash registers, who bought them outright from the Michigan company and resold them, to discontinue the business by threats of interference. A similar transaction to this took place prior to the three years, *i.e.* in 1908. As to the Dial in one instance an agent of the National happening in the office of that company when an acquaintance was there negotiating for some of its stock advised him not to buy it; and in another the plaintiff in error Muzzy attempted to purchase the business or patents of the company which was unsuccessful. We think the court erred in admitting this evidence. The government does not contend that the evidence as to the Dial was sufficient to make a case for the jury of conspir-

acy against it and we have held that that as to the Michigan was not sufficient for that purpose. If this evidence did not tend to establish a conspiracy against those companies, it did not tend to establish one against the American.

We come now to the evidence as to transactions prior to the three years as far back as the beginning of the twenty years which was admitted over defendants' objection and the rulings as to which are assigned as error. The bulk of the evidence relates to such transactions and most of it was objected to. If the admission of any of the evidence as to acts against the American prior to the three years which, we have theretofore stated, is assigned as error, the assignment has escaped us. The admission of the evidence as to the other act against the Michigan is assigned as error. This assignment is well taken for the reason given as to the act within the three years. The rest of the assignments here have to do with evidence tending to show a conspiracy against the competitors who ceased to exist prior to 1907 and a generic conspiracy which was directed against them. The same objections are made to some of this evidence which were made to the evidence of the acts against the American within the three years heretofore set forth. It is urged that the transactions to which it relates do not come within the means specified and the eleventh item is not sufficient to warrant evidence of them under the Greene case. And the defendants were not shown to be connected with or responsible for them. It is also urged as to the evidence relating to transactions and matters occurring in the early part of the twenty years that they were too remote. We think, however, that none of it was too remote. It as well as the evidence of later transactions and matters tended to show a generic conspiracy and bore on its fixed and absolute character and on its nature otherwise. As to defendants' connection therewith they all occurred in the regular course of the business of the National and whether any of the defendants and which of them were connected therewith was open to inference to be drawn by the jury.

Nor do we think the objection to certain of this evidence that it did not relate to transactions coming within the means specified well taken. The ruling of the court in refusing to require

a bill of particulars of the means intended to be covered cannot be questioned here and the indictment was quite liberal in the matter of specification. Besides the case for which the defendants were subject to conviction was limited to means specified, to wit, fifth and ninth. The question here is whether in establishing the generic conspiracy — a fact relevant to the existence of the specific conspiracy covered by that case — the government was limited to the means specified as to competitors who ceased their existence prior to 1907. The tendency of the use of other means than those specified was to establish that the generic conspiracy was to use every possible wrongful means that might be effective in putting an end to competition.

Special emphasis is made upon the assignments which call in question rulings admitting evidence concerning the purchase of the businesses of sixteen competitors by the National prior to 1907, and how the purchases came about. But all this evidence was admissible. Its tendency was to establish a generic conspiracy to compel competitors to sell out to the National by the use of any effective wrongful means in existence when the American came in the field, and the tendency of such generic conspiracy is to establish a specific conspiracy against the American when it came into existence, which continued into the three years, at least to restrain its trade and commerce, if not to compel it to sell out to the National, by the use of the fifth and ninth items. It is true that, at the time of these purchases, suits for infringement were pending against most, if not all, of these competitors. If such suits were brought in good faith and were the cause of the competitors selling out, then the tendency of that evidence was not to establish such a generic conspiracy. The case of *Virtue* v. *Creamery Packing Company*, 227 U. S. 8, 33 Sup. Ct. 202, 57 L. Ed. 393, was an action for treble damages under the seventh section of the Anti-Trust Act for a conspiracy in restraint of the plaintiff's interstate trade by prosecuting suits against them for infringement of patents and circulating reports that his articles were an infringement thereof. Two suits for infringement had been brought, in one of which infringement was denied and in the other decreed. In connection with those suits such reports were circulated. It was held that no recovery could be had.

Mr. Justice McKenna said:

> Patents would be of little value if infringers of them could not be notified of the consequences of infringement or proceeded against in the courts. Such action considered by itself cannot be said to be illegal. Patent rights, it is true, may be asserted in malicious prosecutions as other rights . . . may be. But this is not an action for malicious prosecution. It is an action under the Sherman Anti-Trust Act for the violations . . . of that act, seeking treble damages.

He did not mean by that that no recovery could be had under that act for damages caused by a conspiracy in restraint of interstate trade by the malicious prosecution of suits for infringement. He meant no more than that it did not appear that there was any such conspiracy in that case. So far as appeared, both suits were brought in good faith.

But here there was evidence tending to show that suits were not brought in good faith, and, on the contrary, were an "illicit use of the courts as instrumentalities of oppression," condemned in the case of *Commercial Acetylene Co.* v. *Avery Portable Light Co.* (C. C.) 152 Fed. 642. Besides, there was evidence tending to show in certain of the cases, at least, that the bringing of the suit was not the real cause of the competitors selling out, but the use of other wrongful means. In addition to this, in each case of purchase it was made a provision in the contract that the competitor should not engage in the cash register business for twenty or twenty-five years, except one or two states in the West, where the cash register business was not large, which evidenced the purpose to keep competitors out of the business. This circumstance made what is known as the Leland contract, settling litigation growing out of the suit against the Boston company, in which the National was successful, admissible in evidence. After the end of that suit the National brought suits against certain officers of the Boston to recover damages. In the case of *National Cash Register Co.* v. *Leland,* 94 Fed. 502, 37 C. C. A. 372, it was held that it was entitled to recover, and this is the litigation in settlement of which the contract referred to was executed. By it the National acquired patents, models, and certain apparatus of the Boston company. It contained a provision by

which the officers were not to engage in the cash register business for twenty-five years, except in Montana and Idaho. There was no error in admitting any of these contracts in evidence.

The admission of contracts with others than the competitors named in the indictment, eliminating them from the cash register field, is also assigned as error. There were five or six instances of this kind. The parties with whom the contracts were made were mainly dealers in second-hand registers. They evidence a purpose to acquire complete control of the business in second-hand registers of its make, and were admissible as tending to show a generic conspiracy and its character, notwithstanding they were not referred to in the indictment.

The ground of objection to the evidence thus far considered is at bottom want of relevancy. Except to the extent stated we have found it to be relevant. In addition to these portions of the evidence, the admission of certain other evidence is assigned as error on the ground of its being hearsay. It is evidence as to what took place at two conventions of district managers held at Dayton, one in December, 1902, and the other in July, 1907. We have made use of what was said by the defendant John H. Patterson at the last of the two. What took place at these conventions was evidenced by what purported to be minutes thereof. Those of the first convention were identified by a witness who had been assistant to the head of the competition department and was present at it. He further testified that the minutes were taken by stenographers, amongst whom was the plaintiff in error Harnad, who took most of them, and that he thought a copy was sent to each district manager, and several were kept in the competition department. Those of the last one were identified by the former district manager at Detroit. He testified that they were sent to him by the National company with his name on it. It is not clear whether he is to be understood as testifying that he was present at the convention. Two objections are made to that evidence. One is that both were copies, and the originals should have been produced or accounted for. The other is that the evidence of what took place at those conventions was hearsay. The first objection was not made in the lower court. That raised by the other was that before the minutes

were read in evidence their accuracy should have been guaranteed, either by the persons who made them or by others who were present at the conventions. Strictly speaking, the objection that the evidence was hearsay raised this question. But the objection should have been more specific. It should have been expressly urged that such guaranty should be made before admitting the minutes in evidence. It might have been furnished. Because of this, if any error was committed in admitting these minutes in evidence, it cannot be considered.

This brings us to the assignments questioning rulings excluding evidence offered by the defendants. That mainly complained of is the rejection of evidence offered to prove that the National owned unexpired patents covering the machines made and sold or offered to be sold, by the sixteen competitors whom it bought out, by the Hallwood, International, and Hubinger & Carroll, which quit business, and by the American of Columbus, during the times they were in existence, which machines, therefore, infringed those patents. According to this offer, all the competitors who ceased business prior to 1907, and the American of Columbus, against whose trade and commerce defendants are charged with conspiring, were infringers of the National's patents, and in so conspiring they were but seeking to prevent them from doing that which the National had a right to have them refrain from doing. We are not much impressed with the good faith of the offer as to the American. The conduct of the National and its managing officers during the five years of its existence preceding the indictment seems to belie it. During that time no suit for infringement was brought against that company, except the one heretofore referred to, and there is no indication that they then thought that it was liable to such suit. It is not likely that they would have remained quiescent in this regard, if they so thought. Because of the absence of any evidence to this effect, we have held that the conspiracy as to that company, if there was one, did not include the sixth and seventh means. But, assuming that the offer was made in good faith, we think the court was right in excluding the evidence. It could not have been admissible to meet a charge that it had in bad faith threatened to bring suits for infringement. There was

no such charge to meet. The only possible ground for its admissibility was to make good that defendants had the right to conspire in restraint of the interstate trade and commerce in cash registers of the American by the use of the fifth and ninth means, and hence were not guilty of an offense under first section of the Anti-Trust Act in so doing.

This brings before us the question whether a patentee and another, or the officers and agents of a patentee, can conspire in restraint of the interstate trade or commerce in the article covered by the patent of persons who have no right to engage in such trade and commerce, and who by engaging therein infringe the right of the patentee; *i.e.* whether such a conspiracy comes within that section. Its disposition involves the rights of a patentee. These rights are two, one statutory, and the other at common law. The statutory right is usually stated in its adjective form; *i.e.* to exclude or to prevent others from making, using, or selling the article covered by the patent, or, in other words, to sue or to bring actions against others who are or have been making, using, or selling them. But this right has also a substantive form. It is that others shall refrain from making, or using, or selling the article. The patentee's right at common law is to make, use, or sell the article. This right is to no extent dependent on the statute. The patentee, therefore, has the right to have others refrain from selling the article covered by his patent, and if they will not do so he has the right to prevent them from selling by suit. Has a patentee, then, the right to prevent any infringer from selling the article covered by his patent in any other way? He certainly has no right to do it by killing him, or destroying his factory, or such infringing articles as he may own. In selling the infringing article, no assaults are made upon his person, so that there is no room for claiming that his action was in self-defense. And the infringer owns his factory and articles. The patentee may be entitled to a destruction of the infringing articles through the process of the court, but not otherwise. But has he the right to prevent him from so doing by action outside of the courts, not involving an invasion of the rights of person or property of the infringer; *i.e.* by the use of means which would be wrongful if used by him to prevent another from

selling articles not covered by his patent—*i.e.* such means as are charged here.

We are not concerned here with the question as to what a patentee may himself do in a general way to protect the substantive right which he has from invasion. The question in hand is whether he and another, or his officers and agents in his interest, may conspire to prevent an invasion of his rights in the interstate field by the use of any such means. This depends solely on whether such a conspiracy is within the first section of the Anti-Trust Act. And it would seem that to ask this question is to answer it. The terms of the section are of a most sweeping character. It includes every conspiracy in restraint of interstate trade or commerce. It is not a question whether it is rightful or wrongful interstate trade or commerce that is covered by the conspiracy. It is sufficient that it is interstate trade or commerce. If two or more persons in no way interested in a patent were to conspire in restraint of the interstate trade or commerce of an infringer, no one would contend that the conspiracy was not covered by the statute. No more is it open to contend that a conspiracy by a patentee and another, or by the officers and agents of a patentee in his interest, to restrain the interstate trade or commerce of an infringer, is not within the statute. The intent of the statute was to sweep away all conspiracies in restraint of such trade or commerce, whatever their character may be. The statute respects the monopoly of the patentee. It to no extent invades the rights conferred upon him by his patent. *Bement* v. *National Harrow Co.*, 186 U. S. 70, 22 Sup. Ct. 747, 46 L. Ed. 1058; *United States* v. *Winslow*, 227 U. S. 202, 33 Sup. Ct. 253, 57 L. Ed. 481. But the right to conspire with another or others in his interest in restraint of the interstate trade or commerce covered by his patent is not one of the rights conferred thereby, and such a conspiracy is within the statute. *Standard Sanitary Mfg. Co.* v. *United States.* [Decision reprinted at p. 606, *supra.*] Mr. Justice McKenna there said:

Rights conferred by patents are indeed very definite and extensive, but they do not give any more than other rights a universal license against positive prohibitions. The Sherman Law is a limitation of

rights — rights which may be pushed to evil consequences, and therefore restrained.

We are therefore clearly of the opinion that the defendants were not entitled to offer evidence that the trade and commerce of the American of Columbus in cash registers was covered by an unexpired patent owned by the National.

How, then, as to the competitors who ceased to exist prior to 1907, and who either sold out to the National or just quit doing business? Was evidence that their trade and commerce was covered by unexpired patents so owned admissible? We think it was. As to them the question before the jury was not whether the defendants had the right to conspire in restraint of their interstate trade or commerce. The defendants were not on trial for any such conspiracy. The right to prosecute them for such conspiracy had been long before barred by the statute of limitations. But the question was before the jury whether they had conspired against those competitors to restrain their interstate trade or commerce by threatening to bring and bringing in bad faith suits against them for infringement of patents to compel them to sell out to the National or quit the business. It was the position of the government that they had so conspired, and there was evidence tending to establish that they had, at least as to some of them. This was not an ultimate question in the case. It was only a subordinate one, and yet it was a real one. It was not primarily subordinate to the question whether the defendants had conspired in restraint of the interstate trade or commerce of the American of Columbus by the use of such means. As we have seen, there was no such question in the case. It was primarily subordinate to the question whether, prior to 1907, when the American came into existence, the defendants were parties to a generic conspiracy in restraint of the interstate trade or commerce of all competitors who might endanger the supremacy of the National by the use of any effective means, of which a conspiracy against the American of Columbus by the use of the fifth and ninth means, which continued into the three years, was the outgrowth.

Now, as bearing on that question, we think that the defendants were entitled to prove, if they could, that the machines of

those competitors were infringements. The means covered by the seventh item were in effect malicious prosecutions against those competitors — the bringing of suits for infringement, not in the belief that the National had a good cause of action against them, but without regard to whether it had or not — in order to drive them from the cash register field; *i.e.* in bad faith or without probable cause. A suit for malicious prosecution cannot be brought until the termination of the prosecution. In such a suit, therefore, it is never a question whether there was real cause for the prosecution. Its dismissal settles the question whether there was real cause. But it is a question therein whether there was probable cause. The suit cannot be maintained if there was. But here there was no termination of the suits for infringement, by a decision of the question of infringement involved therein. In most instances the suits were terminated by settlement. The question, therefore, whether there was real cause for bringing them, is still an open question. And if there was real cause for their bringing, they were not malicious prosecutions — they were not brought in bad faith. If in an ordinary suit for malicious prosecution it is a good defense that there was probable cause for the prosecution, so here the claim that these infringement suits were brought in bad faith is met by showing that there was real cause for them, in that the competitors were infringers of valid unexpired patents held by the National. The defendants were not limited to showing that the National acted on the advice of counsel in bringing the suits. They had the right to show, if they could, that such suits were based upon valid patents against real infringers. It is true that the effect of this is to bring into this prosecution a considerable number of patent suits as it were. But the government has brought them here by charging in the indictment that defendants conspired to drive these competitors from the cash register field by maliciously bringing suits for infringements of patents against them, and introducing evidence to that effect. We think, therefore, that the evidence was admissible, and that there was error in excluding it.

It is also urged that the court erred in excluding evidence of competitive tactics and aggressions on the part of the National's

competitors, offered by defendants. As we make it, this evidence related only to the Hallwood, the American's predecessor, and to Steubenrauch, the American's Connecticut sales agent; the conduct of the latter happening within the three years. We think this evidence was admissible. The relevancy of the government's evidence as to a conspiracy against the Hallwood was in its bearing on the existence of a generic conspiracy and its character. The tendency of the evidence as to its competitive tactics and aggressions against the National was to make out that, in so far as there was a conspiracy against the Hallwood, it was due to provocation. Provocation, therefore, was a possible element in the generic conspiracy, and, if so, the fact of there having been no provocation on the part of the American, the remote successor of the Hallwood, would make it open to contend that the general conspiracy was never directed against it. It is in this way that it seems to us that the evidence as to the conduct of the Hallwood bore on the question whether there was a conspiracy against the American. Then, as to Steubenrauch's conduct: The tendency thereof was to show that the conduct of the National's sales agent complained of was due to that conduct, and not to a conspiracy on the part of the defendants against the American.

Finally, the exclusion of the letters of plaintiffs in error High and Snyder to the plaintiff in error Pflum, of date, respectively, April 5, 1909, and April 6, 1909, in answer to his circular letter of April 1, 1909, to the district managers, heretofore quoted in full, are assigned as error. In those letters these two plaintiffs in error stated that the policy therein outlined had been pursued in their districts. We think the letters were admissible in evidence. They were written nearly three years before the finding of the indictment, and were a part of the *res gestæ*. *Hibbard* v. *United States*, 172 Fed. 66, 70, 96 C. C. A. 554, 18 Ann. Cas. 1040; *Harrison* v. *United States*, 200 Fed. 674, 119 C. C. A. 78; *Gould* v. *United States*, 209 Fed. 730, 126 C. C. A. 454. If there was anything in the circumstances then or theretofore existing affecting their good faith, they were for the jury to consider, just as it was for them to determine the good faith of the Pflum circular.

5. It remains to consider the errors assigned in connection with the charge to the jury. But few exceptions were taken to charge which was given, and no assignment of error in this connection has been argued. We therefore pass these exceptions by. The court submitted all three counts to the jury. The defendants requested that the jury be instructed to find them not guilty on the second and third. In accordance with our holding as to the sufficiency of these two counts, the defendants were entitled to have the jury so instructed. The first count alone should have been submitted to them.

The court clearly told the jury that the defendants could not be found guilty under that count unless they had conspired within the three years. This, of course, limited the case upon which they could be so found to competitors in existence during the three years. But defendants were entitled to have the jury instructed specifically that they could not be found guilty as to the competitors who ceased to exist before 1907. They asked specific instructions to this effect. These instructions were given as to six of them. They should have been given as to the other twenty. That such instructions were given as to six made it more prejudicial that they were not given as to the other twenty.

The defendants also requested that the jury be specifically instructed that they could not be found guilty as to each of the six competitors who were in existence during the three years. They were not entitled to the instruction as to the American of Columbus. They were entitled to the instruction as to the other five. There was no substantial evidence that within the five years defendants had conspired as to either of those five competitors. The instructions as to the Burdick-Corbin and Jewell were given. Those also as to the Peninsular, Dial, and Michigan should have been given. The defendants further requested that the jury be specifically instructed that they could not be found guilty of having conspired within the three years in restraint by the use of each of the eleven means specified. They were so instructed as to the fourth. They were entitled to have it instructed also as to the sixth, seventh, eighth, ninth, and eleventh. Whilst, as we have held, the first, second, and third means were non-effec-

tive, without more, and the evidence as to the conspiracy within the three years including either of those means was slight yet such as it was the jury was entitled to consider in connection with that bearing on the fifth and ninth means, and no instructions should have been given which could be construed as excluding that evidence. That it is reversible error to submit to the jury the question whether the conspiracy in question includes means of which there is no evidence follows from the decision in *Nash* v. *United States*, 229 U. S. 373, 33 Sup. Ct. 780, 57 L. Ed. 1232. The grounds upon which we hold the court erred in not giving the specific instructions indicated appear in what we have had to say on defendants' right to a peremptory instruction. The giving of them would have presented sharply to the jury the only ultimate question before it, to wit, whether within the three years the defendants conspired in restraint of the interstate trade or commerce in cash registers of the American of Columbus by the use of the fifth and ninth means specified.

The defendants also requested the giving of three instructions embodying certain general propositions as to what it was not unlawful for the defendants to do in their several capacities as officers and agents of the National, to wit:

(1) To require the agents of their company to report the names of persons who had purchased cash registers from competitors, or to secure samples of machines from time to time put on the market by competitors.

(2) To sell or offer and try to sell National cash registers to persons who had bought and owned competing cash registers in exchange at such price as was satisfactory to the parties.

(3) To compare by comparative demonstrations or otherwise competitive cash registers with National cash registers, for the purpose of demonstrating the superiority of the National cash registers, and thereby induce the prospective purchaser to purchase the National cash register.

No objection can be made to the last proposition, but the other two were too broad. They need qualification. It was unlawful for defendants to do as stated in the second proposition, if the doing thereof involved the purchaser and owner of the compet-

ing cash register breaking his contract with the competitor in any particular, or was done for the purpose of driving the competitor out of the cash register field. One competitor has the right to try to sell by fair means all of his goods that he can, and if the effect of his selling is to drive another competitor out of the field he is not to blame. But it is wrong for one competitor to want to drive another competitor from the field by unfair or illegal means, and to take steps to that end, so that he may have the field free from such competition and thereby be enabled to sell his goods.

Then, as to reporting purchasers of competing registers and securing samples, it all depends on the manner in which the information in the one instance and the samples in the other were obtained or secured. If in a proper manner, nothing unlawful was done.

We do not deem it necessary to consider the other requests asked and refused.

We are constrained, therefore, to reverse the judgment of the lower court, and remand the case for a new trial and further proceedings consistent herewith.

A detail set forth in the government's petition and established by evidence does not appear in this opinion. It is further proof of the predatory tactics employed. A display room was maintained in the factory at Dayton, known as the "Graveyard," wherein were exhibited all the machines which had been "knocked out." Cards were attached to each register, giving dates, amount of money lost and similar discouraging information. This was a prominent feature of the intimidation program. Obstinate competitors were invited to visit Dayton and were escorted through this gruesome exhibit. — *Ed.*

XIX

AMENDMENT OF THE SHERMAN ACT, 1914[1]

After years of public agitation the Anti-Trust Law of 1890 was at last supplemented by two statutes enacted in 1914 after seven months of debate, in fulfillment of the campaign pledges of the Democratic party, and even more particularly, of President Wilson. This legislation was initiated by a Presidential Message on January 20, 1914, accompanying five proposed bills, fashioned upon the lines of the "Seven Sisters" laws in New Jersey. These five measures finally simmered down to the two, known respectively as the Trade Commission Law and the Clayton Anti-Trust Act.

The first four sections of the Trade Commission Law require little explanation. They merely prescribe the form of the commission, its manner of succession to the Bureau of Corporations, and similar routine details. Outwardly the administrative body created closely resembled the Interstate Commerce Commission. It is in the 5th section [together with section 11 of the Clayton Act] that the real innovation in the whole scheme of trust regulation resides. The gist of the entire matter lies here. For while, as will soon appear, the Clayton Act prohibited certain specific unfair practices, such as price discrimination and exclusive tying contracts, section 5 of the Trade Commission Law, in terms as sweeping as those of the Interstate Commerce Act in condemning all unreasonable railroad rates, declares "unfair methods of competition in commerce unlawful." This is the section which transforms the Trade Commission from a merely investigatory body like its predecessor the Bureau of Corporations, into an administrative agency clothed with extended and, as I believe, necessary, police power. This authority it may exercise in the public interest generally, for the good of all rather than to satisfy the claims of an aggrieved plaintiff, whenever it has reason to believe that any unfair method of competition is being employed. In other words, it is intended to promote the standardization of business practice upon a higher and always a decent plane.

As for the machinery for enforcement, as well as the penalties, the details are set forth in sections 5 and 6, — as well as in the Clayton Act, soon to be

[1] Consult *American Economic Review*, Vol. IV, 1915, pp. 839–855, and Vol. V, 1915, pp. 38–54; *Quarterly Journal of Economics*, Vol. XXIX, 1914, pp. 72–97; *Journal of Political Economy*, Vol. XXIII, 1915, pp. 201–220, 305–326, and 417–436.

described. New powers to initiate investigation; to prescribe forms of accounting, such as shall, for instance, be really illuminating as to the relative costs of production under various forms of industrial organization; to classify such reports, according to the needs in each case; and to coöperate with the Department of Justice in detecting and punishing offenders; all of these powers and functions make the Trade Commission law an experiment of the first importance in the exercise of state authority for the promotion of upright, straightforward and sportsmanlike competition — a competition which shall stifle neither opportunity nor efficiency. To seek this end by means of the administrative arm of the government acting in a quasi-judicial capacity, rather than, as under the Sherman Act, by the agency of the courts alone, is quite in consonance with the tendency of the times. The evident aim is to secure a speedier, more direct, and essentially economic, rather than technically legal, determination of vexatious matters of business. Stevens — foremost among authorities on the subject — does not overstate the case in the conclusion[1] that the Trade Commission Act is "an important step . . . toward the ultimate solution of the trust problem." Given a fair field and no secret or discriminatory favors, and competition may well be relied upon to maintain or even to reëstablish itself in the face of impersonal and so often unwieldy monopoly. But the success of this plan, it should be added, depends more directly upon the tact and ability of the members of the commission than upon many verbal details of the law itself. Pettifogging membership may easily wreck the experiment; a broad statesmanlike personnel may lead it on to success. — ED.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That a commission is hereby created and established, to be known as the Federal Trade Commission (hereinafter referred to as the commission), which shall be composed of five commissioners, who shall be appointed by the President, by and with the advice and consent of the Senate. Not more than three of the commissioners shall be members of the same political party. The first commissioners appointed shall continue in office for terms of three, four, five, six, and seven years, respectively, from the date of the taking effect of this Act, the term of each to be designated by the President, but their successors shall be appointed for terms of seven years, except that any person chosen to fill a vacancy shall be appointed only for the unex-

[1] *American Economic Review*, Vol. IV, 1915, p. 854.

pired term of the commissioner whom he shall succeed. The commission shall choose a chairman from its own membership. No commissioner shall engage in any other business, vocation, or employment. Any commissioner may be removed by the President for inefficiency, neglect of duty, or malfeasance in office. A vacancy in the commission shall not impair the right of the remaining commissioners to exercise all the powers of the commission.

The commission shall have an official seal, which shall be udicially noticed.

SEC. 2. That each commissioner shall receive a salary of $10,000 a year, payable in the same manner as the salaries of the judges of the courts of the United States. The commission shall appoint a secretary, who shall receive a salary of $5000 a year, payable in like manner, and it shall have authority to employ and fix the compensation of such attorneys, special experts, examiners, clerks, and other employees as it may from time to time find necessary for the proper performance of its duties and as may be from time to time appropriated for by Congress.

With the exception of the secretary, a clerk to each commissioner, the attorneys, and such special experts and examiners as the commission may from time to time find necessary for the conduct of its work, all employees of the commission shall be a part of classified civil service, and shall enter the service under such rules and regulations as may be prescribed by the commission and by the Civil Service Commission.

All of the expenses of the commission, including all necessary expenses for transportation incurred by the commissioners or by their employees under their orders, in making any investigation, or upon official business in any other places than in the city of Washington, shall be allowed and paid on the presentation of itemized vouchers therefor approved by the commission.

Until otherwise provided by law, the commission may rent suitable offices for its use.

The Auditor for the State and Other Departments shall receive and examine all accounts of expenditures of the commission.

SEC. 3. That upon the organization of the commission and election of its chairman, the Bureau of Corporations and the offices of Commissioner and Deputy Commissioner of Corporations shall cease to exist; and all pending investigations and proceedings of the Bureau of Corporations shall be continued by the commission.

All clerks and employees of the said bureau shall be transferred to and become clerks and employees of the commission at their present grades and salaries. All records, papers, and property of the said bureau shall become records, papers, and property of the commission, and all unexpended funds and appropriations for the use and maintenance of the said bureau, including any allotment already made to it by the Secretary of Commerce from the contingent appropriation for the Department of Commerce for the fiscal year nineteen hundred and fifteen, or from the departmental printing fund for the fiscal year nineteen hundred and fifteen, shall become funds and appropriations available to be expended by the commission in the exercise of the powers, authority, and duties conferred on it by this Act.

The principal office of the commission shall be in the city of Washington, but it may meet and exercise all its powers at any other place. The commission, may, by one or more of its members, or by such examiners, as it may designate, prosecute any inquiry necessary to its duties in any part of the United States.

SEC. 4. That the words defined in this section shall have the following meaning when found in this Act, to wit:

"Commerce" means commerce among the several States or with foreign nations, or in any Territory of the United States or in the District of Columbia, or between any such Territory and another, or between any such Territory and any State or foreign nation, or between the District of Columbia and any State or Territory or foreign nation.

"Corporation" means any company or association incorporated or unincorporated, which is organized to carry on business for profit and has shares of capital or capital stock, and any company or association, incorporated or unincorporated, without shares of capital or capital stock, except partnerships,

which is organized to carry on business for its own profit or that of its members.

"Documentary evidence" means all documents, papers, and correspondence in existence at and after the passage of this Act.

"Acts to regulate commerce" means the act entitled "An Act to regulate commerce," approved February fourteenth, eighteen hundred and eighty-seven, and all acts amendatory thereof and supplementary thereto.

"Anti-trust acts" means the Act entitled "An Act to protect trade and commerce against unlawful restraints and monopolies," approved July second, eighteen hundred and ninety; also the sections seventy-three to seventy-seven, inclusive, of an Act entitled "An Act to reduce taxation, to provide revenue for the Government, and for other purposes," approved August twenty-seventh, eighteen hundred and ninety-four; and also the Act entitled "An Act to amend sections seventy-three and seventy-six of the Act of August twenty-seventh, eighteen hundred and ninety-four, entitled 'An Act to reduce taxation, to provide revenue for the Government, and for other purposes,'" approved February twelfth, nineteen hundred and thirteen.

SEC. 5. That unfair methods of competition in commerce are hereby declared unlawful.

The commission is hereby empowered and directed to prevent persons, partnerships, or corporations, except banks, and common carriers subject to the Acts to regulate commerce, from using unfair methods of competition in commerce.

Whenever the commission shall have reason to believe that any such person, partnership, or 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 person, partnership, or corporation a complaint stating its charges in that respect, and containing a notice of a hearing upon a day and at a place therein fixed at least thirty days after the service of said complaint. The person, partnership, or corporation so complained of shall have the right to appear at the place and time so fixed and show cause why an order should not be entered by the commission requiring such

person, partnership, or corporation to cease and desist from the violation of the law so charged in said complaint. Any person, partnership, or corporation may make application, and upon good cause shown may be allowed by the commission, to intervene and appear in said proceeding by counsel or in person. The testimony in any such proceeding shall be reduced to writing and filed in the office of the commission. If upon such hearing the commission shall be of the opinion that the method of competition in question is prohibited by this Act, it shall make a report in writing in which it shall state its findings as to the facts, and shall issue and cause to be served on such person, partnership, or corporation an order requiring such person, partnership, or corporation to cease and desist from using such method of competition. Until a transcript of the record in such hearing shall have been filed in a circuit court of appeals of the United States, as hereinafter provided, the commission may at any time, upon such notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any report or any order made or issued by it under this section.

If such person, partnership, or corporation fails or neglects to obey such order of the commission while the same is in effect, the commission may apply to the circuit court of appeals of the United States, within any circuit where the method of competition in question was used or where such person, partnership, or corporation resides or carries on business, for the enforcement of its order, and shall certify and file with its application a transcript of the entire record in the proceeding, including all the testimony taken and the report and order of the commission. Upon such filing of the application and transcript the court shall cause notice thereof to be served upon such person, partnership, or corporation and thereupon shall have jurisdiction of the proceeding and of the question determined therein, and shall have power to make and enter upon the pleadings, testimony, and proceedings set forth in such transcript a decree affirming, modifying, or setting aside the order of the commission. The findings of the commission as to the facts, if supported by testimony, shall be conclusive. If either party shall apply to the court for leave to adduce additional evidence, and

shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for the failure to adduce such evidence in the proceeding before the commission, the court may order such additional evidence to be taken before the commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The commission may modify its findings as to the facts, or make new findings, by reason of the additional evidence so taken, and it shall file such modified or new findings, which, if supported by testimony, shall be conclusive, and its recommendation, if any, for the modification or setting aside of its original order, with the return of such additional evidence. The judgment and decree of the court shall be final, except that the same shall be subject to review by the Supreme Court upon *certiorari* as provided in section two hundred and forty of the Judicial Code.

Any party required by such order of the commission to cease and desist from using such method of competition may obtain a review of such order in said circuit court of appeals by filing in the court a written petition praying that the order of the commission be set aside. A copy of such petition shall be forthwith served upon the commission, and thereupon the commission forthwith shall certify and file in the court a transcript of the record as hereinbefore provided. Upon the filing of the transcript the court shall have the same jurisdiction to affirm, set aside, or modify the order of the commission as in the case of an application by the commission for the enforcement of its order, and the findings of the commission as to the facts, if supported by testimony, shall in like manner be conclusive.

The jurisdiction of the circuit court of appeals of the United States to enforce, set aside, or modify orders of the commission shall be exclusive.

Such proceedings in the circuit court of appeals shall be given precedence over other cases pending therein, and shall be in every way expedited. No order of the commission or judgment of the court to enforce the same shall in any wise relieve or absolve any person, partnership, or corporation from any liability under the anti-trust acts.

Complaints, orders, and other processes of the commission under this section may be served by any one duly authorized by the commission, either (*a*) by delivering a copy thereof to the person to be served, or to a member of the partnership to be served, or to the president, secretary, or other executive officer or a director of the corporation to be served; or (*b*) by leaving a copy thereof at the principal office or place of business of such person, partnership, or corporation; or (*c*) by registering or mailing a copy thereof addressed to such person, partnership, or corporation at his or its principal office or place of business. The verified return by the person so serving said complaint, order, or other process setting forth the manner of said service shall be proof of the same, and the return post-office receipt for said complaint, order, or other process registered and mailed as aforesaid shall be proof of the service of the same.

Sec. 6. That the commission shall also have power —

(*a*) To gather and compile information concerning, and to investigate from time to time the organization, business, conduct, practices, and management of any corporation engaged in commerce, excepting banks and common carriers subject to the Act to regulate commerce, and its relation to other corporations and to individuals, associations, and partnerships.

(*b*) To require, by general or special orders, corporations engaged in commerce, excepting banks, and common carriers subject to the Act to regulate commerce, or any class of them, or any of them, respectively, to file with the commission in such form as the commission may prescribe annual or special, or both annual and special, reports or answers in writing to specific questions, furnishing to the commission such information as it may require as to the organization, business, conduct, practices, management, and relation to other corporations, partnerships, and individuals of the respective corporations filing such reports or answers in writing. Such reports and answers shall be made under oath, or otherwise, as the commission may prescribe, and shall be filed with the commission within such reasonable period as the commission may prescribe, unless additional time be granted in any case by the commission.

(*c*) Whenever a final decree has been entered against any

defendant corporation in any suit brought by the United States to prevent and restrain any violation of the anti-trust Acts, to make investigation, upon its own initiative, of the manner in which the decree has been or is being carried out, and upon the application of the Attorney-General it shall be its duty to make such investigation. It shall transmit to the Attorney-General a report embodying its findings and recommendations as a result of any such investigation, and the report shall be made public in the discretion of the commission.

(*d*) Upon the direction of the President or either House of Congress to investigate and report the facts relating to any alleged violations of the anti-trust Acts by any corporation.

(*e*) Upon the application of the Attorney General to investigate and make recommendations for the readjustment of the business of any corporation alleged to be violating the anti-trust Acts in order that the corporation may thereafter maintain its organization, management, and conduct of business in accordance with law.

(*f*) To make public from time to time such portions of the information obtained by it hereunder, except trade secrets and names of customers, as it shall deem expedient in the public interest; and to make annual and special reports to the Congress and to submit therewith recommendations for additional legislation; and to provide for the publication of its reports and decisions in such form and manner as may be best adapted for public information and use.

(*g*) From time to time to classify corporations and to make rules and regulations for the purpose of carrying out the provisions of this Act.

(*h*) To investigate, from time to time, trade conditions in and with foreign countries where associations, combinations, or practices of manufacturers, merchants, or traders, or other conditions, may affect the foreign trade of the United States, and to report to Congress thereon, with such recommendations as it deems advisable.

SEC. 7. That in any suit in equity brought by or under the direction of the Attorney-General as provided in the anti-trust Acts, the court may, upon the conclusion of the testimony therein,

if it shall be then of opinion that the complainant is entitled to relief, refer said suit to the commission, as a master in chancery, to ascertain and report an appropriate form of decree therein. The commission shall proceed upon such notice to the parties and under such rules of procedure as the court may prescribe, and upon the coming in of such report such exceptions may be filed and such proceedings had in relation thereto as upon the report of a master in other equity causes, but the court may adopt or reject such report, in whole or in part, and enter such decree as the nature of the case may in its judgment require.

SEC. 8. That the several departments and bureaus of the government when directed by the President shall furnish the commission, upon its request, all records, papers, and information in their possession relating to any corporation subject to any of the provisions of this Act, and shall detail from time to time such officials and employees to the commission as he may direct.

SEC. 9. That for the purposes of this Act the commission, or its duly authorized agent or agents, shall at all reasonable times have access to, for the purpose of examination, and the right to copy any documentary evidence of any corporation being investigated or proceeded against; and the commission shall have power to require by subpœna the attendance and testimony of witnesses and the production of all such documentary evidence relating to any matter under investigation. Any member of the commission may sign subpœnas, and members and examiners of the commission may administer oaths and affirmations, examine witnesses, and receive evidence.

Such attendance of witnesses, and the production of such documentary evidence, may be required from any place in the United States, at any designated place of hearing. And in case of disobedience to a subpœna the commission may invoke the aid of any court of the United States in requiring the attendance and testimony of witnesses and the production of documentary evidence.

Any of the district courts of the United States within the jurisdiction of which such inquiry is carried on may, in case of contumacy or refusal to obey a subpœna issued to any corporation or other person, issue an order requiring such corporation

or other person to appear before the commission, or to produce documentary evidence if so ordered, or to give evidence touching the matter in question; and any failure to obey such order of the court may be punished by such court as a contempt thereof.

Upon the application of the Attorney-General of the United States, at the request of the commission, the district courts of the United States shall have jurisdiction to issue writs of mandamus commanding any person or corporation to comply with the provisions of this Act or any order of the commission made in pursuance thereof.

The commission may order testimony to be taken by deposition in any proceeding or investigation pending under this Act at any stage of such proceeding or investigation. Such depositions may be taken before any person designated by the commission and having power to administer oaths. Such testimony shall be reduced to writing by the person taking the deposition, or under his direction, and shall then be subscribed by the deponent. Any person may be compelled to appear and depose and to produce documentary evidence in the same manner as witnesses may be compelled to appear and testify and produce documentary evidence before the commission as hereinbefore provided.

Witnesses summoned before the commission shall be paid the same fees and mileage that are paid witnesses in the courts of the United States, and witnesses whose depositions are taken and the persons taking the same shall severally be entitled to the same fees as are paid for like services in the courts of the United States.

No person shall be excused from attending and testifying or from producing documentary evidence before the commission or in obedience to the subpœna of the commission on the ground or for the reason that the testimony or evidence, documentary or otherwise, required of him may tend to criminate him or subject him to a penalty or forfeiture. But no natural person shall be prosecuted or subjected to any penalty or forfeiture for or on account of any transaction, matter, or thing concerning which he may testify, or produce evidence, documentary or otherwise,

before the commission in obedience to a subpœna issued by it: *Provided*, That no natural person so testifying shall be exempt from prosecution and punishment for perjury committed in so testifying.

SEC. 10. That any person who shall neglect or refuse to attend and testify, or to answer any lawful inquiry, or to produce documentary evidence, if in his power to do so, in obedience to the subpœna or lawful requirement of the commission, shall be guilty of an offense and upon conviction thereof by a court of competent jurisdiction shall be punished by a fine of not less than $1000, nor more than $5000, or by imprisonment for not more than one year, or by both such fine and imprisonment.

Any person who shall willfully make, or cause to be made, any false entry or statement of fact in any report required to be made under this Act, or who shall willfully make, or cause to be made, any false entry in any account, record, or memorandum kept by any corporation subject to this Act, or who shall willfully neglect or fail to make, or to cause to be made, full, true, and correct entries in such accounts, records, and memoranda of all facts and transactions appertaining to the business of such corporation, or who shall willfully remove out of the jurisdiction of the United States, or willfully mutilate, alter, or by any other means falsify any documentary evidence of such corporation, or who shall willfully refuse to submit to the commission or to any of its authorized agents, for the purpose of inspection and taking copies, any documentary evidence of such corporation in his possession or within his control, shall be deemed guilty of an offense against the United States, and shall be subject, upon conviction in any court of the United States of competent jurisdiction, to a fine of not less than $1000 nor more than $5000, or to imprisonment for a term of not more than three years, or to both such fine and imprisonment.

If any corporation required by this Act to file any annual or special report shall fail so to do within the time fixed by the commission for filing the same, and such failure shall continue for thirty days after notice of such default, the corporation shall forfeit to the United States the sum of $100 for each and every day of the continuance of such failure, which forfeiture shall be

payable into the Treasury of the United States, and shall be recoverable in a civil suit in the name of the United States brought in the district where the corporation has its principal office or in any district in which it shall do business. It shall be the duty of the various district attorneys, under the direction of the Attorney-General of the United States, to prosecute for the recovery of forfeitures. The costs and expenses of such prosecution shall be paid out of the appropriation for the expenses of the courts of the United States.

Any officer or employee of the commission who shall make public any information obtained by the commission without its authority, unless directed by a court, shall be deemed guilty of a misdemeanor, and, upon conviction thereof, shall be punished by a fine not exceeding $5000 or by imprisonment not exceeding one year, or by fine and imprisonment, in the discretion of the court.

SEC. 11. Nothing contained in this Act shall be construed to prevent or interfere with the enforcement of the provisions of the anti-trust Acts or the Acts to regulate commerce, nor shall anything contained in the Act be construed to alter, modify, or repeal the said anti-trust Acts or Acts to regulate commerce or any part or parts thereof.

Approved, September 26, 1914.

THE CLAYTON ACT

The Clayton Act "to supplement existing laws against unlawful restraints and monopolies," — that is to say, the Sherman Anti-Trust Law. — is a hodge-podge, compounded of various details, many unnecessary, some conflicting, others positively mischievous. It is the expression of an honest popular purpose to remedy existing economic evils and to fulfill Democratic campaign pledges. But it is a broth which clearly suffers from too many cooks; or, to change figures, a hammer which aims to hit too many nails on the head at one and the same time. Unfair trade practices, interlocking directorates, intercorporate stockholdings, dishonest railroad financing, the legal status of trade-unions and even the use of injunctions in labor disputes, are all comprehended within the statute. Our attention, naturally, must be focused upon those features of the act which deal specifically with the preservation of an open market and a fair field for all comers in business. Yet it is probable that many of these details of the law represent a compromise, that is to say, a give-and-take between opposing groups in Congress. Without the contempt

of court and injunction sections, approval of the restraint of trade clauses would probably have failed of support from the labor vote. One may hesitate perhaps to follow Professor Young to the extent of characterizing the Clayton Act as "bungling and generally futile." One may with greater confidence assent to Stevens' conclusion that, so far as amendment of the Sherman Act is concerned, "no harm has been done;" and in certain details, such as the prohibition of tying arrangements, the new legislation was rendered necessary by instant decisions of the Supreme Court of the United States.

Turning to the text of the statute, section 2 specifically prohibits price discrimination between different purchasers of commodities. This was obviously aimed at such tactics as local price cutting, so successfully utilized by the Standard Oil Company to build up its monopoly. But it will be observed that this statute enables the suppression of such acts, not merely when incidental to the creation of monopoly but at all times and under all circumstances. If price cutting be not advantageous to the community in general, as the better economic opinion now holds, a real addition to the Sherman Act has been made hereby. But whether the same end had not already been achieved in the general prohibition of unfair business practices in the Trade Commission Law, is at least debatable. It is also open to question whether the permission to vary prices "in good faith to meet competition" may not open the door to nullification of the entire section and possibly to weaken the Sherman Act itself. Whether it will do so or not, depends upon how constructively the courts virtually legislate in interpretation of the statute. Section 3 of the law contains another specific prohibition, supplementary, or it may be, defining to that extent, both the Sherman Act and the Trade Commission Law. For it declares unlawful, all exclusive or tying clauses, such as have been employed by the United Shoe Machinery Company in its leases of machinery, by the Thread and Photographic combinations in their selling agreements with jobbers and retailers, or by the electric lamp pool in its purchasing contracts. In view of recent pronouncements of the United States Supreme Court in patent decisions, notably in the Dick case, a clear definition of the rights of traders would seem to have been needed. Section 5 is an important one, in that it relieves the plaintiff in a suit for damages under the Act, of proof of the offense, if that has already once been established in a Federal proceeding. The following sections 6, 7, 8, 9, and 10 have to do with matters only incidentally related to the trust problem. The prohibition of intercorporate stockholdings reverts to the issue of the holding company already discussed in connection with the Northern Securities case; while the restrictions upon interlocking directorates touch the subtle details of credit and banking facilities. Section 9 dealing with common carriers resulted from the disclosures in the New Haven and Rock Island scandals of the time.[1]

[1] Ripley, Railroads: Finance and Organization, pp. 471, 524, etc.

The remainder of the Act deals with procedure, enforcement and penalties. Much of it is highly technical. It appears to be bungling, where, for example, it provides for *final* decision upon the prohibitions of the Act by both the Supreme Court and the Circuit Court of Appeals. It provides for duplication and possible conflict of authority by vesting enforcement in the Department of Justice as well as in the Trade Commission. It will also be noted that the omission of all criminal penalties, as have been ineffectively imposed in a few instances in the past, rests everything upon the employment of contempt of court procedure in future. The provision in section 14, whereby the act of a corporation shall be deemed that of its directors, would seem to express a need of the time, — a need, however, so apparent that the courts seem independently in a fair way to solve the difficulty without recourse to the new statute. Section 11 of the Clayton Act, as we have already noted, dovetails into section 5 of the Trade Commission Law, and needs to be considered in connection with it.

Whatever the shortcomings of the measure, one cannot withhold admiration for the steadfastness of purpose, the worthiness of motive and the extraordinary political ability of President Wilson in achieving this fulfillment of the pledges of his party in the face of seemingly insuperable difficulties.— ED.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That "anti-trust laws," as used herein, includes the Act entitled "An Act to protect trade and commerce against unlawful restraints and monopolies," approved July second, eighteen hundred and ninety; sections seventy-three to seventy-seven, inclusive, of an Act entitled "An Act to reduce taxation, to provide revenue for the Government, and for other purposes," of August twenty-seventh, eighteen hundred and ninety-four; an Act entitled "An Act to amend sections seventy-three and seventy-six of the Act of August twenty-seventh, eighteen hundred and ninety-four, entitled 'An Act to reduce taxation, to provide revenue for the Government, and for other purposes,'" approved February twelfth, nineteen hundred and thirteen; and also this Act.

"Commerce," as used herein, means trade or commerce among the several States and with foreign nations, or between the District of Columbia or any Territory of the United States and any State, Territory, or foreign nation, or between any insular possessions or other places under the jurisdiction of the United States, or between any such possession or place and any State

or Territory of the United States or the District of Columbia or any foreign nation, or within the District of Columbia or any Territory or any insular possession or other place under the jurisdiction of the United States: *Provided*, That nothing in this Act contained shall apply to the Philippine Islands.

The word "person" or "persons" wherever used in this Act shall be deemed to include corporations and associations existing under or authorized by the laws of either the United States, the laws of any of the Territories, the laws of any State, or the laws of any foreign country.

SEC. 2. That it shall be unlawful for any person engaged in commerce, in the course of such commerce, either directly or indirectly to discriminate in price between different purchasers of commodities which commodities are sold for use, consumption, or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, where the effect of such discrimination may be to substantially lessen competition or tend to create a monopoly in any line of commerce: *Provided*, That nothing herein contained shall prevent discrimination in price between purchasers of commodities on account of differences in the grade, quality, or quantity of the commodity sold, or that makes only due allowance for difference in the cost of selling or transportation, or discrimination in price in the same or different communities made in good faith to meet competition: *And provided further*, That nothing herein contained shall prevent persons engaged in selling goods, wares, or merchandise in commerce from selecting their own customers in *bona fide* transactions and not in restraint of trade.

SEC. 3. That it shall be unlawful for any person engaged in commerce, in the course of such commerce, to lease or make a sale or contract for sale of goods, wares, merchandise, machinery, supplies or other commodities, whether patented or unpatented, for use, consumption or resale within the United States or any Territory thereof or the District of Columbia or any insular possession or other place under the jurisdiction of the United States, or fix a price charged therefor, or discount from, or rebate upon, such price, on the condition, agreement or understanding that

the lessee or purchaser thereof shall not use or deal in the goods, wares, merchandise, machinery, supplies or other commodities of a competitor or competitors of the lessor or seller, where the effect of such lease, sale, or contract for sale or such condition, agreement or understanding may be to substantially lessen competition or tend to create a monopoly in any line of commerce.

SEC. 4. That any person who shall be injured in his business or property by reason of anything forbidden in the anti-trust laws may sue therefor in any district court in the United States in the district in which the defendant resides or is found or has an agent, without respect to the amount in controversy, and shall recover threefold the damages by him sustained, and the cost of suit, including a reasonable attorney's fee.

SEC. 5. That a final judgment or decree hereafter rendered in any criminal prosecution or in any suit or proceeding in equity brought by or on behalf of the United States under the anti-trust laws to the effect that a defendant has violated said laws shall be *prima facie* evidence against such defendant in any suit or proceeding brought by any other party against such defendant under said laws as to all matters respecting which said judgment or decree would be an estoppel as between the parties thereto: *Provided*, This section shall not apply to consent judgments or decrees entered before any testimony has been taken: *Provided further*, This section shall not apply to consent judgments or decrees rendered in criminal proceedings or suits in equity, now pending, in which the taking of testimony has been commenced but has not been concluded, provided such judgments or decrees are rendered before any further testimony is taken.

Whenever any suit or proceeding in equity or criminal prosecution is instituted by the United States to prevent, restrain or punish violations of any of the anti-trust laws, the running of the statute of limitations in respect of each and every private right of action arising under said laws and based in whole or in part on any matter complained of in said suit or proceeding shall be suspended during the pendency thereof.

SEC. 6. That the labor of a human being is not a commodity or article of commerce. Nothing contained in the anti-trust laws shall be construed to forbid the existence and operation of labor,

agricultural, or horticultural organizations, instituted for the purposes of mutual help, and not having capital stock or conducted for profit, or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the anti-trust laws.

SEC. 7. That no corporation engaged in commerce shall acquire, directly or indirectly the whole or any part of the stock or other share capital of another corporation engaged also in commerce, where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce.

No corporation shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of two or more corporations engaged in commerce where the effect of such acquisition, or the use of such stock by the voting or granting of proxies or otherwise, may be to substantially lessen competition between such corporations, or any of them, whose stock or other share capital is so acquired, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce.

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, or in attempting to bring about, the substantial lessening of competition. Nor shall anything contained in this section prevent a corporation engaged in commerce from causing the formation of subsidiary corporations for the actual carrying on of their immediate 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, when the effect of such formation is not to substantially lessen competition.

Nor shall anything herein contained be construed to prohibit any common carrier subject to the laws to regulate commerce from aiding in the construction of branches or short lines so

located as to become feeders to the main line of the company so aiding in such construction or from acquiring or owning all or any part of the stock of such branch lines, nor to prevent any such common carrier from acquiring and owning all or any part of the stock of a branch or short line constructed by an independent company where there is no substantial competition between the company owning the branch line so constructed and the company owning the main line acquiring the property or an interest therein, nor to prevent such common carrier from extending any of its lines through the medium of the acquisition of stock or otherwise of any other such common carrier where there is no substantial competition between the company extending its lines and the company whose stock, property, or an interest therein is so acquired.

Nothing contained in this section shall be held to affect or impair any right heretofore legally acquired: *Provided*, That nothing in this section shall be held or construed to authorize or make lawful anything heretofore prohibited or made illegal by the anti-trust laws, nor to exempt any person from the penal provisions thereof or the civil remedies therein provided.

SEC. 8. That from and after two years from the date of the approval of this Act no person shall at the same time be a director or other officer or employee of more than one bank, banking association or trust company, organized or operating under the laws of the United States, either of which has deposits, capital, surplus, and undivided profits aggregating more than $5,000,000; and no private banker or person who is a director in any bank or trust company, organized and operating under the laws of a State, having deposits, capital, surplus, and undivided profits aggregating more than $5,000,000, shall be eligible to be a director in any bank or banking association organized or operating under the laws of the United States. The eligibility of a director, officer, or employee under the foregoing provisions shall be determined by the average amount of deposits, capital, surplus, and undivided profits as shown in the official statements of such bank, banking association, or trust company filed as provided by law during the fiscal year next preceding the date set for the annual election of directors, and

when a director, officer, or employee has been elected or selected in accordance with the provisions of this Act it shall be lawful for him to continue as such for one year thereafter under said election or employment.

No bank, banking association or trust company, organized or operating under the laws of the United States, in any city or incorporated town or village of more than two hundred thousand inhabitants, as shown by the last preceding decennial census of the United States, shall have as a director or other officer or employee any private banker or any director or other officer or employee of any other bank, banking association or trust company located in the same place: *Provided*, That nothing in this section shall apply to mutual savings banks not having a capital stock represented by shares: *Provided further*, That a director or other officer or employee of such bank, banking association, or trust company may be a director or other officer or employee of not more than one other bank or trust company organized under the laws of the United States or any State where the entire capital stock of one is owned by stockholders in the other: *And provided further*, That nothing contained in this section shall forbid a director of class A of a Federal reserve bank, as defined in the Federal Reserve Act from being an officer or director or both an officer and director in one member bank.

That from one and after two years from the date of the approval of this Act no person at the same time shall be a director in any two or more corporations, any one of which has capital, surplus, and undivided profits aggregating more than $1,000,000, engaged in whole or in part in commerce, other than banks, banking associations, trust companies and common carriers subject to the Act to regulate commerce, approved February fourth, eighteen hundred and eighty-seven, if such corporations are or shall have been theretofore, by virtue of their business and location of operation, competitors, so that the elimination of competition by agreement between them would constitute a violation of any of the provisions of any of the anti-trust laws. The eligibility of a director under the foregoing provision shall be determined by the aggregate amount of the

capital, surplus, and undivided profits, exclusive of dividends declared but not paid to stockholders, at the end of the fiscal year of said corporation next preceding the election of directors, and when a director has been elected in accordance with the provisions of this Act it shall be lawful for him to continue as such for one year thereafter.

When any person elected or chosen as a director or officer or selected as an employee of any bank or other corporation subject to the provisions of this Act is eligible at the time of his election or selection to act for such bank or other corporation in such capacity his eligibility to act in such capacity shall not be affected and he shall not become or be deemed amenable to any of the provisions hereof by reason of any change in the affairs of such bank or other corporation from whatsoever cause, whether specifically excepted by any of the provisions hereof or not, until the expiration of one year from the date of his election or employment.

SEC. 9. Every president, director, officer or manager of any firm, association or corporation engaged in commerce as a common carrier, who embezzles, steals, abstracts or willfully misapplies, or willfully permits to be misapplied, any of the moneys, funds, credits, securities, property or assets of such firm, association or corporation, arising or accruing from, or used in, such commerce, in whole or in part, or willfully or knowingly converts the same to his own use or to the use of another, shall be deemed guilty of a felony and upon conviction shall be fined not less than $500 or confined in the penitentiary not less than one year nor more than ten years, or both, in the discretion of the court.

Prosecutions hereunder may be in the district court of the United States for the district wherein the offense may have been committed.

That nothing in this section shall be held to take away or impair the jurisdiction of the courts of the several States under the laws thereof; and a judgment of conviction or acquittal on the merits under the laws of any State shall be a bar to any prosecution hereunder for the same act or acts.

SEC. 10. That after two years from the approval of this Act

no common carrier engaged in commerce shall have any dealings in securities, supplies or other articles of commerce, or shall make or have any contracts for construction or maintenance of any kind, to the amount of more than $50,000, in the aggregate, in any one year, with another corporation, firm, partnership or association when the said common carrier shall have upon its board of directors or as its president, manager or as its purchasing or selling officer, or agent in the particular transaction, any person who is at the same time a director, manager, or purchasing or selling officer of, or who has any substantial interest in, such other corporation, firm, partnership or association, unless and except such purchases shall be made from, or such dealings shall be with, the bidder whose bid is the most favorable to such common carrier, to be ascertained by competitive bidding under regulations to be prescribed by rule or otherwise by the Interstate Commerce Commission. No bid shall be received unless the name and address of the bidder or the names and addresses of the officers, directors and general managers thereof, if the bidder be a corporation, or of the members, if it be a partnership or firm, be given with the bid.

Any person who shall, directly or indirectly, do or attempt to do anything to prevent anyone from bidding or shall do any act to prevent free and fair competition among the bidders or those desiring to bid shall be punished as prescribed in this section in the case of an officer or director.

Every such common carrier having any such transactions or making any such purchases shall within thirty days after making the same file with the Interstate Commerce Commission a full and detailed statement of the transaction showing the manner of the competitive bidding, who were the bidders, and the names and addresses of the directors and officers of the corporations and the members of the firm or partnership bidding; and whenever the said commission shall, after investigation or hearing, have reason to believe that the law has been violated in and about the said purchases or transactions it shall transmit all papers and documents and its own views of findings regarding the transaction to the Attorney General.

If any common carrier shall violate this section it shall be

fined not exceeding $25,000; and every such director, agent, manager or officer thereof who shall have knowingly voted for or directed the act constituting such violation or who shall have aided or abetted in such violation shall be deemed guilty of a misdemeanor and shall be fined not exceeding $5,000, or confined in jail not exceeding one year, or both, in the discretion of the court.

SEC. 11. That authority to enforce compliance with sections two, three, seven and eight of this Act by the persons respectively subject thereto is hereby vested: in the Interstate Commerce Commission where applicable to common carriers, in the Federal Reserve Board where applicable to banks, banking associations and trust companies, and in the Federal Trade Commission where applicable to all other character of commerce, to be exercised as follows:

Whenever the commission or board vested with jurisdiction thereof shall have reason to believe that any person is violating or has violated any of the provisions of sections two, three, seven and eight of this Act, it shall issue and serve upon such person a complaint stating its charges in that respect, and containing a notice of a hearing upon a day and at a place therein fixed at least thirty days after the service of said complaint. The person so complained of shall have the right to appear at the place and time so fixed and show cause why an order should not be entered by the commission or board requiring such person to cease and desist from the violation of the law so charged in said complaint. Any person may make application, and upon good cause shown may be allowed by the commission or board, to intervene and appear in said proceeding by counsel or in person. The testimony in any such proceeding shall be reduced to writing and filed in the office of the commission or board. If upon such hearing the commission or board, as the case may be, shall be of the opinion that any of the provisions of said sections have been or are being violated, it shall make a report in writing in which it shall state its findings as to the facts, and shall issue and cause to be served on such person an order requiring such person to cease and desist from such violations, and divest itself of the stock held or rid itself of the

directors chosen contrary to the provisions of sections seven and eight of this Act, if any there be, in the manner and within the time fixed by said order. Until a transcript of the record in such hearing shall have been filed in a circuit court of appeals of the United States, as hereinafter provided, the commission or board may at any time, upon such notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any report or any order made or issued by it under this section.

If such person fails or neglects to obey such order of the commission or board while the same is in effect, the commission or board may apply to the circuit court of appeals of the United States, within any circuit where the violation complained of was or is being committed or where such person resides or carries on business, for the enforcement of its order, and shall certify and file with its application a transcript of the entire record in the proceeding, including all the testimony taken and the report and order of the commission or board. Upon such filing of the application and transcript the court shall cause notice thereof to be served upon such person and thereupon shall have jurisdiction of the proceeding and of the question determined therein, and shall have power to make and enter upon the pleadings, testimony, and proceedings set forth in such transcript a decree affirming, modifying, or setting aside the order of the commission or board. The findings of the commission or board as to the facts, if supported by testimony, shall be conclusive. If either party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for the failure to adduce such evidence in the proceeding before the commission or board, the court may order such additional evidence to be taken before the commission or board and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The commission or board may modify its findings as to the facts, or make new findings, by reason of the additional evidence so taken, and it shall file such modified or new findings, which, if supported by testimony, shall be conclusive, and its recommendation, if any, for the modification or setting

aside of its original order, with the return of such additional evidence. The judgment and decree of the court shall be final, except that the same shall be subject to review by the Supreme Court upon *certiorari* as provided in section two hundred and forty of the Judicial Code.

Any party required by such order of the commission or board to cease and desist from a violation charged may obtain a review of such order in said circuit court of appeals by filing in the court a written petition praying that the order of the commission or board be set aside. A copy of such petition shall be forthwith served upon the commission or board, and thereupon the commission or board forthwith shall certify and file in the court a transcript of the record as hereinbefore provided. Upon the filing of the transcript the court shall have the same jurisdiction to affirm, set aside, or modify the order of the commission or board as in the case of an application by the commission or board for the enforcement of its order, and the findings of the commission or board as to the facts, if supported by testimony, shall in like manner be conclusive.

The jurisdiction of the circuit court of appeals of the United States to enforce, set aside, or modify orders of the commission or board shall be exclusive.

Such proceedings in the circuit court of appeals shall be given precedence over other cases pending therein, and shall be in every way expedited. No order of the commission or board or the judgment of the court to enforce the same shall in any wise relieve or absolve any person from any liability under the antitrust Acts.

Complaints, orders, and other processes of the commission or board under this section may be served by anyone duly authorized by the commission or board, either (*a*) by delivering a copy thereof to the person to be served, or to a member of the partnership to be served, or to the president, secretary, or other executive officer or a director of the corporation to be served; or (*b*) by leaving a copy thereof at the principal office or place of business of such person; or (*c*) by registering and mailing a copy thereof addressed to such person at his principal office or place of business. The verified return by the person so serving

said complaint, order, or other process setting forth the manner of said service shall be proof of the same, and the return post-office receipt for said complaint, order, or other process registered and mailed as aforesaid shall be proof of the service of the same.

SEC. 12. That any suit, action, or proceeding under the antitrust laws against a corporation may be brought not only in the judicial district whereof it is an inhabitant, but also in any district wherein it may be found or transacts business; and all process in such cases may be served in the district of which it is an inhabitant, or wherever it may be found.

SEC. 13. That in any suit, action, or proceeding brought by or on behalf of the United States subpœnas for witnesses who are required to attend a court of the United States in any judicial district in any case, civil or criminal, arising under the antitrust laws may run into any other district: *Provided*, That in civil cases no writ of subpœna shall issue for witnesses living out of the district in which the court is held at a greater distance than one hundred miles from the place of holding the same without the permission of the trial court being first had upon proper application and cause shown.

SEC. 14. That whenever a corporation shall violate any of the penal provisions of the antitrust laws, such violation shall be deemed to be also that of the individual directors, officers, or agents of such corporation who shall have authorized, ordered, or done any of the acts constituting in whole or in part such violation, and such violation shall be deemed a misdemeanor, and upon conviction therefor of any such director, officer, or agent he shall be punished by a fine of not exceeding $5,000 or by imprisonment for not exceeding one year, or by both, in the discretion of the court.

SEC. 15. That the several district courts of the United States are hereby invested with jurisdiction to prevent and restrain violations of this Act, and it shall be the duty of the several district attorneys of the United States, in their respective districts, under the direction of the Attorney General, to institute proceedings in equity to prevent and restrain such violations. Such proceedings may be by way of petition setting forth the

case and praying that such violation shall be enjoined or otherwise prohibited. When the parties complained of shall have been duly notified of such petition, the court shall proceed, as soon as may be, to the hearing and determination of the case; and pending such petition, and before final decree, the court may at any time make such temporary restraining order or prohibition as shall be deemed just in the premises. Whenever it shall appear to the court before which any such proceeding may be pending that the ends of justice require that other parties should be brought before the court, the court may cause them to be summoned whether they reside in the district in which the court is held or not, and subpœnas to that end may be served in any district by the marshal thereof.

SEC. 16. That any person, firm, corporation, or association shall be entitled to sue for and have injunctive relief, in any court of the United States having jurisdiction over the parties, against threatened loss or damage by a violation of the antitrust laws, including sections two, three, seven and eight of this Act, when and under the same conditions and principles as injunctive relief against threatened conduct that will cause loss or damage is granted by courts of equity, under the rules governing such proceedings, and upon the execution of proper bond against damages for an injunction improvidently granted and a showing that the danger of irreparable loss or damage is immediate, a preliminary injunction may issue: *Provided*, That nothing herein contained shall be construed to entitle any person, firm, corporation, or association, except the United States, to bring suit in equity for injunctive relief against any common carrier subject to the provisions of the Act to regulate commerce, approved February fourth, eighteen hundred and eighty-seven, in respect of any matter subject to the regulation, supervision, or other jurisdiction of the Interstate Commerce Commission.

SEC. 17. That no preliminary injunction shall be issued without notice to the opposite party.

No temporary restraining order shall be granted without notice to the opposite party unless it shall clearly appear from specific facts shown by affidavit or by the verified bill that immediate and irreparable injury, loss, or damage will result to the

applicant before notice can be served and a hearing had thereon. Every such temporary restraining order shall be indorsed with the date and hour of issuance, shall be forthwith filed in the clerk's office and entered of record, shall define the injury and state why it is irreparable and why the order was granted without notice, and shall by its terms expire within such time after entry, not to exceed ten days, as the court or judge may fix, unless within the time so fixed the order is extended for a like period for good cause shown, and the reasons for such extension shall be entered of record. In case a temporary restraining order shall be granted without notice in the contingency specified, the matter of the issuance of a preliminary injunction shall be set down for a hearing at the earliest possible time and shall take precedence of all matters except older matters of the same character; and when the same comes up for hearing the party obtaining the temporary restraining order shall proceed with the application for a preliminary injunction, and if he does not do so the court shall dissolve the temporary restraining order. Upon two days' notice to the party obtaining such temporary restraining order the opposite party may appear and move the dissolution or modification of the order, and in that event the court or judge shall proceed to hear and determine the motion as expeditiously as the ends of justice may require.

Section two hundred and sixty-three of an Act entitled "An Act to codify, revise, and amend the laws relating to the judiciary," approved March third, nineteen hundred and eleven, is hereby repealed.

Nothing in this section contained shall be deemed to alter, repeal, or amend section two hundred and sixty-six of an Act entitled "An Act to codify, revise, and amend the laws relating to the judiciary," approved March third, nineteen hundred and eleven.

Sec. 18. That, except as otherwise provided in section sixteen of this Act, no restraining order or interlocutory order of injunction shall issue, except upon the giving of security by the applicant in such sum as the court or judge may deem proper, conditioned upon the payment of such costs and damages as may be incurred or suffered by any party who may be found to have been wrongfully enjoined or restrained thereby.

SEC. 19. That every order of injunction or restraining order shall set forth the reasons for the issuance of the same, shall be specific in terms, and shall describe in reasonable detail, and not by reference to the bill of complaint or other document, the act or acts sought to be restrained, and shall be binding only upon the parties to the suit, their officers, agents, servants, employees, and attorneys, or those in active concert or participating with them, and who shall, by personal service or otherwise, have received actual notice of the same.

SEC. 20. That no restraining order or injunction shall be granted by any court of the United States, or a judge or the judges thereof, in any case between an employer and employees, or between employers and employees, or between employees, or between persons employed and persons seeking employment, involving, or growing out of, a dispute concerning terms or conditions of employment, unless necessary to prevent irreparable injury to property, or to a property right, of the party making the application, for which injury there is no adequate remedy at law, and such property or property right must be described with particularity in the application, which must be in writing and sworn to by the applicant or by his agent or attorney.

And no such restraining order or injunction shall prohibit any person or persons, whether singly or in concert, from terminating any relation of employment, or from ceasing to perform any work or labor, or from recommending, advising, or persuading others by peaceful means so to do; or from attending at any place where any such person or persons may lawfully be, for the purpose of peacefully obtaining or communicating information, or from peacefully persuading any person to work or to abstain from working; or from ceasing to patronize or to employ any party to such dispute, or from recommending, advising, or persuading others by peaceful and lawful means so to do; or from paying or giving to, or withholding from, any person engaged in such dispute, any strike benefits or other moneys or things of value; or from peaceably assembling in a lawful manner, and for lawful purposes; or from doing any act or thing which might lawfully be done in the absence of such dispute by any party thereto; nor shall any of the acts specified

in this paragraph be considered or held to be violations of any law of the United States.

SEC. 21. That any person who shall willfully disobey any lawful writ, process, order, rule, decree, or command of any district court of the United States or any court of the District of Columbia by doing any act or thing therein, or thereby forbidden to be done by him, if the act or thing so done by him be of such character as to constitute also a criminal offense under any statute of the United States, or under the laws of any State in which the act was committed, shall be proceeded against for his said contempt as hereinafter provided.

SEC. 22. That whenever it shall be made to appear to any district court or judge thereof, or to any judge therein sitting, by the return of a proper officer on lawful process, or upon the affidavit of some credible person, or by information filed by any district attorney, that there is reasonable ground to believe that any person has been guilty of such contempt, the court or judge thereof, or any judge therein sitting, may issue a rule requiring the said person so charged to show cause upon a day certain why he should not be punished therefor, which rule, together with a copy of the affidavit or information, shall be served upon the person charged, with sufficient promptness to enable him to prepare for and make return to the order at the time fixed therein. If upon or by such return, in the judgment of the court, the alleged contempt be not sufficiently purged, a trial shall be directed at a time and place fixed by the court: *Provided, however,* That if the accused, being a natural person, fail or refuse to make return to the rule to show cause, an attachment may issue against his person to compel an answer, and in case of his continued failure or refusal, or if for any reason it be impracticable to dispose of the matter on the return day, he may be required to give reasonable bail for his attendance at the trial and his submission to the final judgment of the court. Where the accused is a body corporate, an attachment for the sequestration of its property may be issued upon like refusal or failure to answer.

In all cases within the purview of this Act such trial may be by the court, or, upon demand of the accused, by a jury; in

which latter event the court may impanel a jury from the jurors then in attendance, or the court or the judge thereof in chambers may cause a sufficient number of jurors to be selected and summoned, as provided by law, to attend at the time and place of trial, at which time a jury shall be selected and impaneled as upon a trial for misdemeanor; and such trial shall conform, as near as may be, to the practice in criminal cases prosecuted by indictment or upon information.

If the accused be found guilty, judgment shall be entered accordingly, prescribing the punishment, either by fine or imprisonment, or both, in the discretion of the court. Such fine shall be paid to the United States or to the complainant or other party injured by the act constituting the contempt, or may, where more than one is so damaged, be divided or apportioned among them as the court may direct, but in no case shall the fine to be paid to the United States exceed, in case the accused is a natural person, the sum of $1,000, nor shall such imprisonment exceed the term of six months: *Provided*, That in any case the court or a judge thereof may, for good cause shown, by affidavit or proof taken in open court or before such judge and filed with the papers in the case, dispense with the rule to show cause, and may issue an attachment for the arrest of the person charged with contempt; in which event such person, when arrested, shall be brought before such court or a judge thereof without unnecessary delay and shall be admitted to bail in a reasonable penalty for his appearance to answer to the charge or for trial for the contempt; and thereafter the proceedings shall be the same as provided herein in case the rule had issued in the first instance.

SEC. 23. That the evidence taken upon the trial of any persons so accused may be preserved by bill of exceptions, and any judgment of conviction may be reviewed upon writ of error in all respects as now provided by law in criminal cases, and may be affirmed, reversed, or modified as justice may require. Upon the granting of such writ of error, execution of judgment shall be stayed, and the accused, if thereby sentenced to imprisonment, shall be admitted to bail in such reasonable sum as may be required by the court, or by any justice, or any judge of any

district court of the United States or any court of the District of Columbia.

SEC. 24. That nothing herein contained shall be construed to relate to contempts committed in the presence of the court, or so near thereto as to obstruct the administration of justice, nor to contempts committed in disobedience of any lawful writ, process, order, rule, decree, or command entered in any suit or action brought or prosecuted in the name of, or on behalf of, the United States, but the same, and all other cases of contempt not specifically embraced within section twenty-one of this Act, may be punished in conformity to the usages at law and in equity now prevailing.

SEC. 25. That no proceeding for contempt shall be instituted against any person unless begun within one year from the date of the act complained of; nor shall any such proceeding be a bar to any criminal prosecution for the same act or acts; but nothing herein contained shall affect any proceedings in contempt pending at the time of the passage of this Act.

SEC. 26. If any clause, sentence, paragraph, or part of this Act shall, for any reason, be adjudged by any court of competent jurisdiction to be invalid, such judgment shall not affect, impair, or invalidate the remainder thereof, but shall be confined in its operation to the clause, sentence, paragraph, or part thereof directly involved in the controversy in which such judgment shall have been rendered.

Approved, October 15, 1914.

XX

THE LAW CONCERNING MONOPOLISTIC COMBINATIONS IN CONTINENTAL EUROPE[1]

THE problem of monopolistic combinations in industry is of world-wide character, but the law respecting them differs greatly in the most important states. These differences arise partly from various historical circumstances of social and legal development, but they are also due to different views as to the significance of such combinations and the attitude that the state should assume towards them with respect to both public and private interests.

Industrial combinations are by no means purely modern phenomena, and the jurisprudence of Europe in ancient as well as in modern times has addressed itself to the question of their propriety and legality. In the early empire, for example, the law made the cornering and engrossing of grain a criminal offense, and threatened the same with penalties varying from a denial of trading privileges to banishment and public labor. A law of Zeno, under the later empire, forbade under penalty of a heavy fine all combinations whereby it was agreed that a commodity should not be sold below a certain price. A similar policy was followed in the middle ages by the emperors of the Holy Roman Empire, and by the kings of France, and to their influence can be traced some of the provisions of modern European codes.

The course of development in modern states has not only differed widely, but in the same state, at different periods, the changing views of political and social philosophy have been reflected in the law. A remarkable illustration of the effect of new ideas is seen in the legislation of the French Revolution, and notably in the law which forbade all associations in the form known to the French law as "corporations" (*i.e.* guilds or as-

[1] *Political Science Quarterly*, Vol. XX, 1905, pp. 13–41. Elaborate footnotes and references to cases are omitted for lack of space.

sociations of persons in the same trade) on account of the odious monopolies which they had established under the *ancien régime*. Another illustration of more historical importance, and resting on deeper rooted ideas of social policy, is found in the nineteenth century movement towards industrial freedom which has brought about the abolition of laws prohibiting employers and wage-earners from combining with respect to labor contracts. In this matter, indeed, the policies of modern states, following a strong democratic tendency, have shown more consistency than with respect to combinations to control production and prices. It is with this last question that we are here concerned.

The evolution and present condition of combinations in Europe is quite beyond the scope of this discussion; it is sufficient to say that, taking the continent as a whole, industrial combinations seem quite as numerous as in America and in some countries they are highly developed. They are usually called cartells. The European cartell corresponds to an American pool, but it is generally more highly organized. Consolidated organizations of business — trusts, fusions, mergers, etc. — are rarely found.

The conditions of space and material make it necessary to confine the discussion of the law to the chief industrial countries of continental Europe, viz., Germany, Austria, and France, although brief references will be made to certain others. For these three states it is possible to make a fairly complete statement of the law, although no attempt will be made to enter into the minute distinctions of legal interpretation nor to give an exhaustive digest of the cases. One phase of the subject, the regulation of competition in bidding on public contracts, will be omitted entirely.

The law can be most conveniently examined and clearly understood by taking each country separately, considering, first, the criminal law, and, second, the civil law, and examining under each (*a*) legislation, (*b*) judicial decisions and (*c*) comment of jurists.

I. The German Empire

The law of the German Empire is of special interest for two reasons: first, because the new code represents the latest effort of scientific jurisprudence and, second, because it was established

at a time when industrial combinations had reached a high stage of development in that country and had attracted the attention of statesmen and jurists.

The German criminal code contains no prohibition against cartells nor any law specially concerning them. A good many offenses under the criminal law might, of course, be committed by cartells. A case of some interest occurred recently under the article of the criminal code which prohibits extortion. A powder manufacturing combination refused to supply dealers who did not buy exclusively of them. One of their customers purchased supplies from an outsider and was threatened in consequence with a discontinuance of supply. The imperial court condemned this as contrary to the law.

The provisions of the civil law in Germany are much more important with respect to cartells than those of the criminal law, but here also nothing is to be found preventing their establishment. The civil law implicitly recognizes the validity of cartell contracts, because it establishes the general principle of freedom of contract, without making any exception of cartell contracts. Cartells have been attacked, nevertheless, in the courts, both under the industrial code and under the civil code.

The industrial code (*Gewerbeordnung*) establishes the general principle of free industry in its first section, which reads: "The pursuit of an industry is permitted to everyone, in so far as exceptions or limitations are not imposed or permitted in the present law." The interpretation of this section goes back to the beginning of the activity of the German imperial court. The earlier cases were regarding such restraints on the freedom of industry as are contained in contracts to abstain from engaging in a certain business under certain conditions of time and space. In a case decided in 1880 the court said: "The industrial code does not aim to limit the freedom of contract to any greater extent than is required in the interest of the public." In 1890 a case came before the imperial court concerning the relations of a publishers' and booksellers' cartell with an outsider, against whom certain discriminations had been made on account of rate-cutting. The cartell was attacked as an infringement of the principle of free industry. The court, however, denied this and said in part:

From the principal of industrial liberty it does not follow that there must be no interference with the free play of economic forces, in the sense that persons engaged in an industry should be prohibited from endeavoring in the way of associated self-help to regulate the activity of these forces and to prevent excesses that are deemed injurious.

The most important decision of all was in the case of the Saxon wood pulp cartell in 1897. In this the court declared that a cartell was not only not contrary to the principle of free industry but was often in the interest of the public as well as of the members of the cartell. As regarded the claim that the cartell was contrary to the principle of industrial liberty, the court said:

This objection cannot, however, be regarded as well founded. The association which appears in this case as plaintiff was established, as is expressly stated in its statutes and is not disputed in the pleadings, in order to prevent in the future a destructive competition between the Saxon wood pulp manufacturers, and to make possible the attainment of higher prices than could be gotten with unrestricted competition.

After noting that associations for such a purpose are often regarded, "especially outside of Germany," as violating the principle of industrial liberty and the public interest which that principle aims to further, the court continued:

If in any branch of industry the prices of the products sink too low, and the thriving operation of the industry is thereby made impossible or endangered, then the crisis which occurs is destructive not only to the individuals but also to the social economy in general, and it lies therefore in the interest of the whole community that immoderately low prices shall not exist permanently in any industry.

Hence the court concluded that cartells are not improper in principle, but it indicated that this conclusion does not justify them absolutely in all cases.

To contracts of the kind under consideration, therefore, exception can be taken from the standpoint of the protection of the general interests through industrial freedom only if in individual cases objections arise from particular circumstances, especially if there is an evident purpose of establishing an actual monopoly and of effecting an usurious exploitation of the consumers, or if these consequences are actually brought about by the agreements and arrangements made.

This last statement is of especial interest, because it shows that the court recognizes at least a theoretical limit to the freedom of combination. This limitation, however, does not seem to have any great practical value, inasmuch as there are various cartells which have organized a practical monopoly and have pursued what may be fairly termed extortionate price policies, in the face of bitter complaint and against litigious parties, without the legality of their constitution being called in question.

It appears, therefore, from the uniform judgments of the imperial court that the cartells are not regarded as infringing the principle of industrial liberty.

Under the civil code the cartell contracts have likewise been declared lawful. There are only two articles of interest here, which reads as follows:

Art. 138. A jural act that is repugnant to morality is void.

Art. 826. Whoever, in a manner repugnant to morality, intentionally inflicts an injury upon another is bound to such other for compensation of the injury.

It does not appear that any efforts have been made to attack the validity of cartell contracts under the first of the above sections (138), but decision was rendered on the same point of law in a number of cases before the present code went into effect. An early cartell case was decided in the highest Bavarian court (*oberstes Landgericht*) in Munich, April 7, 1888. In this case the court declared that a cartell contract of certain tile manufacturers to limit production and fix minimum prices was not only valid, but also a prudent business arrangement. The court denied that either the aim or the means adopted in such an agreement was *contra bonos mores.*

Of much greater importance, because decided in the imperial court, was the case of the book publishers' cartell referred to above. It was claimed that this cartell was contrary to good morals and public order. The court said that such a point of view might be relevant, if it were shown that a combination had been formed to control the market and to check the free play of economic forces for speculative purposes, but went on to say:

A complete distinction should be drawn between such combinations and associations of fellow craftsmen for the purpose, pursued in good

faith, of maintaining an industry on a living basis through protection against depreciation of products and against other disadvantages arising from the price cutting of individuals.

The other article of the civil code (826) cited above might have some application to the malpractices of cartells, but not to their legal existence. A case came up recently wherein a steamship line tried to force a competing line out of a certain trade by refusing to take freight at the ordinary rates from one of its large shippers if he continued to patronize the competing line. The injured shipper brought suit to compel the steamship line to desist from such action. The claim of the plaintiff was sustained in the court of first instance, denied on appeal, but again sustained in the imperial court. The imperial court said, in part:

Article 826 is adapted and also intended by the legislator to establish a protection against unfair treatment in a comprehensive manner, particularly for business intercourse, in so far as provision is not made through special laws.

The court suggested that an action for extortion might lie. It also pointed out that the obligation of a common carrier (*Transportzwang*) was established in Germany for railway transportation only, not for other land carriage, nor for sea carriage; and suggested that such a compulsion might appear to be necessary, especially against enterprises which subserved a public interest and which possessed, legally or *de facto*, a monopoly of such service. Meanwhile, even in the absence of any legal duty to render the service, the arbitrary and unfair refusal of transportation at the ordinary rates was to be regarded as an action *contra bonos mores*. As a standard of morals within the meaning of article 826, the court accepted the sense of propriety (*Anstandsgefühl*), of right-minded persons, and in commercial matters the views and sentiments of honorable business men.

Although this case had no direct relation to the cartells, the position taken by the court is of much interest as showing its attitude towards monopolies and towards practices in which cartels are frequent offenders.

In this connection may be noticed again the case of the book

publishers' cartell. The court denied the claim of the plaintiffs to damages from the cartell upon the ground that the record showed no injury, but it did not decide whether the means used by the cartell against outsiders, viz., total exclusion from supply of books, refusal to furnish the trade journal or to publish advertisements therein, denial of certain rebates and the publication of a black list in the trade journal, were unlawful or not, although it intimated that they were not lawful.

The courts have not only refused to declare cartell contracts illegal, but they have also expressly declared them valid, including the penalty clauses embraced therein for violation of such agreements. Thus, in the above cited Saxon wood pulp cartell, the refusal to pay the conventional fines was declared a breach of a lawful engagement. This decision was made before the code in its present form went into effect, but the same principles were applied as in the recent case regarding the interpretation of the agreement of the coal syndicate. Speaking of this agreement the court said: "against the validity of which well-founded objections do not exist." The court declared that the Hannibal mine must perform its obligations under the agreement, or pay damages. A still more recent case, in which the validity of a cartell agreement was involved, concerned the right of a member to withdraw. The court held the agreement to be a valid one, but declared that a member might withdraw in case the other parties made the proper fulfilment of the contract impossible.

In the opinions of jurists may be found some useful criticism of the meaning and possibilities of the present law. The subject was considered with much minuteness in the twenty-sixth convention of the German jurists in 1902, and was again under consideration at their recent meeting in the autumn of 1904. One of the prominent speakers in the convention in 1902 declared that the existing law was sufficient to prevent objectionable practices, *i.e.* associations aiming at monopoly could be attacked at their establishment under article 138, and in their operation under article 826. Landesberger expressed the opinion that it was possible to test the validity of cartell contracts generally under article 138, and supported his opinion by a

citation from the opinion of the imperial court in the Saxon wood pulp manufacturers' case. He said:

I do not hold it [article 138] as totally inapplicable. Cartell agreements and cartell resolutions of a directly usurious character or acts done in the execution of cartell resolutions which were demonstrably intended to ruin an outsider, might well be characterized as *contra bonos mores.*

He confessed that in any case the article was applicable only in a very limited range of cases. (Rundstein takes a somewhat similar position, holding that article 138 would apply, if cartells possessing a monopoly were guilty of exploiting the public, or if it could be proved that they intended to do so.) Boyens thought that a cartell contract that did not provide a fair arrangement between the members — one, for example, that gave the large members too much power over the small members — might be *contra bonos mores* in the sense of article 138. It is interesting to observe that the original draft of article 138 had a wider scope, invalidating not only jural acts that were repugnant to morality, but also such as were repugnant to public order.

A good deal of hope, in a small way, appears to be put in the provisions of article 826. For example, Juliusberg thinks that boycotting and usurious exploitation through exorbitant prices may be made a ground of action for damages under this article. Boyens claims that intentional underbidding, with the aim of preventing a competitor from working without loss, or of compelling him to enter a cartell, may be attacked under this article as an effort to cause damage to another in an immoral fashion, and that such proceedings may be contested both preventively and repressively. For these reasons, also, a cartell might be declared invalid. Menzel, on the other hand, thinks that article 826 is of little practical significance in opposing cartell excesses, because a judgment can seldom be obtained on account of the difficulty of proving malice (*dolus*).

II. Austria

In no important industrial country in Europe are the laws less favorable to industrial combinations than in Austria, but in

hardly any other country are such combinations more numerous. The laws concerning them were established at a period before they had acquired the significance that they possess to-day, and the application of these older laws to cartell agreements has been sometimes disputed. The policy of the Austrian government has tended recently to increase the restrictions placed on combinations, but the legislative projects in this direction have not been enacted into law.

There are no penal laws against industrial combinations. The penal code of 1852, which in general is still in force, provided that "agreements of persons engaged in industry [*Gewerbsleute*], manufacturers [etc.] . . . to raise the price of a commodity . . . to the disadvantage of the public or to reduce the same to their own advantage or to cause a scarcity," should be punished as misdemeanors. The provisions of this section were abrogated by the law of April 7, 1870, which declared that such agreements should be deemed repugnant to the penal law only in case intimidation or force were used. The Austrian criminal law, therefore, now contains no provisions specially applicable to cartells.

It should be noted, however, that while the law of April 7, 1870, abolished the penalties previously imposed on industrial combinations, it did not legalize them from the point of view of the civil law. On the contrary, article 2 of the law of 1870 declares that certain agreements concerning the giving or taking of employment, etc., "have no legal operation." Article 4 declares: "The provisions contained in articles 1 and 2 have application also to agreements of persons engaged in industry [*Gewerbsleute*] with the purpose of raising the price of a commodity to the disadvantage of the public."

The law of 1870, therefore, made industrial combinations void, but, on account of the character of the law of procedure existing before 1895, this declaration of the statute could be evaded, for most practical purposes, by providing that any matters of dispute in regard to the obligations of the parties to the agreement should be submitted to a private board of arbitration, established by the said agreement. According to the law of procedure existing before 1895, the decisions of such an arbi-

tration were binding and could be annulled in the courts only in case of open fraud. The law of procedure was altered in 1895 by the introduction of a new code, which declares that the decisions of a private court of arbitration are inoperative "if repugnant to compulsory rules of law," and it is provided that parties cannot lawfully renounce their right of appeal to the courts in such cases.

There have been some important judicial decisions in Austria respecting the validity of cartell agreements, interpreting the law of 1870. It is remarkable that no cases came up for decision until within the last decade, and after Professor Menzel had pointed out its application in his celebrated discussion of the subject before the *Verein für Sozial-Politik* in 1894.

The first cartell case to be decided was with respect to a cartell of oleum producers, which had been organized in 1887 for a limited period for the regulation of the sale of oleum, chiefly, though not exclusively, in the export trade. A suit was brought for damages for breach of the terms of the agreement, and the defense was made that the contract was invalid under the law of 1870. The supreme court (*oberster Gerichtshof*) held that the agreement was invalid, and denied the claim for compensation. The court said: "The plaintiff objects, with justice, that such an agreement is without legal operation." The decision of the court depended largely on verbal definitions. The word "*Gewerbsleute*" was held to include every industrial producer, and the word "*Gewerbe*" was held to be applicable to factory production as well as to handicraft. Popular use, it seems, had come to restrict "*Gewerbe*" to the form of industry practiced by petty craftsmen and artisans, but the court pointed out that the term was used in various laws to embrace factory industry and that there was no reason to suppose that the legislator intended to protect the public against the extortion of handicraftsmen only. The court also held that proof of the advance of prices was not necessary, and that a limitation of the agreement in respect to the area or term of operation did not make it lawful.

Another cartell case came before the supreme court of Austria in the following year (1899) concerning a combination among the talc producers (*Federweisscartell*) of Styria, which had established a central selling bureau in Vienna for a term of five years.

Conventional penalties were provided for breach of the agreement. A firm which was a member of the cartell brought an action to obtain a judgment that its contract under the cartell agreement was invalid, but this claim was rejected in the local and provincial courts. The supreme court took the same view as in the case noticed above, and declared the compact void. In regard to prices the court said that it was not necessary to prove that there had been an advance of the same to the disadvantage of the public, but that the intent to raise prices could be deduced from the nature of the agreement. Such an indication of intent appeared in provisions for the limitation of output or for the regulation of prices by a central bureau, etc. The court defined the meaning of the statute further by declaring that the rule applied not only to finished products and articles of daily use, but also to unfinished goods and goods used in production.

We may notice, finally, a third case, which was decided on appeal in a provincial court. The cartell concerned was that of the Austrian enameled utensil producers. The court of original instance declared the cartell contract null and void, but held that the contracts between the cartell members and their agent — the provincial bank — were valid. The upper provincial court denied the validity of all these contracts. The court said in part:

> There is no doubt that the agreement of the plate and enameled utensil cartell has simply the purpose to raise the price of an article of consumption at present necessary and of general use, or to prevent the decline of the same. . . . If the defendants claim, therefore, that they aim simply at the restoration of the market to normal conditions, then that is simply to be understood in the interest of the cartelled firms, but not in the interest of the public. . . . The objection that since the formation of the cartell the retail prices have fallen is irrelevant, according to the coalition law, as regards the legal operation of the cartell.

It seems that the court regarded the contracts between the cartelled producers and the bank which acted as their agent as invalid, on the ground that the general organization fixed the prices and the bank was, in effect, an organ of the cartell and not a third party.

The criticism of jurists is of considerable interest in connection

with the Austrian law. Menzel wrote, in 1894, that "Austria is the only state which possesses an explicit and unambiguous legal norm concerning the validity of cartell agreements." Nevertheless the lower courts have not shown perfect agreement with the supreme court as to the meaning of the law, and some intelligent writers have strongly objected to the position taken by the supreme court. Hitchmann, for example, criticizes the declaration of the court in the talc producers' cartell case, on the following grounds: (1) there was no express price agreement, which he thinks should be necessary to bring it clearly within the prohibition of the law; (2) "*Gewerbsleute*" does not include manufacturers, but designates only petty craftsmen; and (3) the "public" does not mean a particular group of people, but the people generally, who are interested in the prices of consumption goods only.

Grunzel (who is in a measure a representative of the industrial interests) also objects strongly to the interpretation of the law given by the supreme court. He holds with Hitchmann that neither law nor custom warrants applying the term "*Gewerbsleute*" to large corporations. Further, he denies that the existence of a cartell is sufficient evidence of intent to raise prices, and asserts that most cartells do not attempt to raise prices, but try to keep them from falling. He points out that the law expressly states that agreements designed to advance prices are unlawful, and he ridicules the attitude of the court in saying that the proof that retail prices have fallen is irrelevant. He holds also with Hitchmann that the commodities embraced within the meaning of the law are those of general use, and would not include, for example, locomotives or potash.

Still more significant is the statement made in the explanation of motives which accompanied the celebrated Austrian cartell bill of 1897. The representatives of the government expressed doubts as to how far the law of 1870 would be applicable in respect to the validity of cartell agreements. According to the opinion expressed therein, it would not affect: (1) cartells for the maintenance (not increase) of prices; (2) cartells for the depression of the prices of the raw material, whether directly, or indirectly by a *rayon* agreement; and (3) cartells to procure more favorable arrangements as to freights, insurance, etc.

In regard to the question whether prices have been advanced or not, attention should be called to the wording of the statute, which expressly regards aim or purpose (*Zweck*). Rundstein approves of the position taken by the courts that the actual price movement is immaterial.

In spite of the unfavorable attitude of the law, cartells have flourished in Austria almost as vigorously as in Germany. They exist, as Landesberger says, according to the maxim: "Where there is no plaintiff, there is no judge." He says that the cartells might be attacked successfully only if an action by outsiders (*actio popularis*) were allowed, though even such an action would not do much more than procure a formal declaration of nullity. Such agreements exist, in other words, not by virtue of law but on the basis of business convenience and commercial faith and credit — "but only as long as self-preservation is not at stake." Their existence and practical operation depend on the interests of private parties in maintaining or destroying them, so that under the existing law the good ones may be destroyed and the bad ones may survive. The effect of the law of 1870, therefore, according to this authority, is to deprive parties of the right of complaint for the non-observance of cartell agreements, and to make them void in all matters for which the courts have to consider them.[1]

III. FRANCE

The era of the Revolution was marked by the abolition of the ancient *corporations*, *maitrises* or *jurandes*, and by the enactment of severe laws against combination. The law of June 14–17, 1791, denounced agreements of members of the same trade to fix the price of their industry or labor as "unconstitutional, hostile to liberty, and of no effect." On July 26, 1793, the "*loi contre les accapareurs*," *i.e.* the law against engrossers and the like, was adopted, which threatened offenders with the penalties of death and confiscation. Just before this, on May 4, 1793, the famous law of the maximum had been established,

[1] Landesberger, im 26ten Juristentag, pp. 350–355. It is noteworthy that the *Kaufmännischer Verein* of Vienna recently condemned any attempt by a membei of a cartell to escape his contractual obligations by recourse to the courts. *Cf* *Kartell-Rundschau*, 1904, p. 435.

i.e. a law which fixed the maximum price for each of a great variety of articles, in order to afford a prompt remedy against monopoly. Most of the legislation of the Revolution in this direction was of an ephemeral character, but the law against *l'accapasement*, with less severe penalties, was embodied in the penal code of 1810, articles 419 and 420, and has continued to the present day. The more important of these articles reads as follows:

Art. 419. All those who by false or calumnious reports sown by design in the community, by offers of prices in advance of those asked by the vendors themselves, by union or coalition between the principal possessors of the same merchandise or commodity not to sell or to sell at a certain price only, or by whatever fraudulent ways and means, shall have effected the advance or decline of the prices of commodities or merchandise or of public securities above or below the prices which the natural and free competition of trade would have fixed, shall be punished with imprisonment of one month at least or of one year at most and with a fine of five hundred francs to ten thousand francs. The culprits may, further, be placed by decree or judgment under the oversight of the superior police during two years at least and five years at most.

The following article (420) provides heavier penalties if the commodities in question are breadstuffs, bread, or wine or other potables.

Since the adoption of this code, other laws of minor importance have been enacted concerning combinations under particular conditions. For our present purpose, these require no notice. One law, however, not directly concerned with our subject, requires attention, because it has been declared in some quarters to abrogate articles 419 and 420 of the penal code. This is the law of March 21, 1884, concerning the establishment of trade associations. In article 3 of this law, the aim of the associations authorized is defined as follows: "Professional syndicates have for their exclusive aim the study and defense of economic, industrial, commercial or agricultural interests." The courts have held, as seems only reasonable, that this does not permit them to violate a criminal statute from the operation of which they are not expressly excepted.

One of the earliest cases involving the status of cartells under

the criminal code was that of certain soda manufacturers of Marseilles, which was decided in 1838. These manufacturers had formed a combination to sell all their output through the agency of one Mille, who added the precaution of hiring six factories, which were not in operation, in order to prevent the reëstablishment of competition. Prices were advanced about 25 per cent, although the price of the raw material had declined. The court of cassation declared briefly that this combination came within the prohibition of article 419. In a case decided in the same year, the court of cassation declared that a combination of concerns in the form of a fusion or consolidation was not an illegal coalition, within the meaning of that article, because a plurality of persons was necessary, and this was not found in a single juristic person (*personne morale*). In the year following (1839) an action was brought against a coach company, respecting agreements as to the price of places, and the court of cassation declared that the commodities embraced in article 419 included incorporeal as well as corporeal goods.

The following decision illustrates the application of the law where prices are depressed by combination. A case came before the court of cassation in 1879 concerning a combination among the manufacturers of iodine, who employed a common purchasing agent, divided up the field which supplied the raw material, and fixed the prices of the same. The court said that this was a combination, "organized by the principal manufacturers of iodine," tending to give to the commodity prices above or below the course which would have been determined "by the free and natural competition of commerce," and was repugnant, therefore, to article 419 of the penal code and to article 1133 of the civil code.

The earlier judgments of the French courts showed a tendency to interpret and apply article 419 in a comprehensive and effective manner. The modern tendency has been less rigorous. The opinion of the court of Paris in the following case is a good illustration of this statement. It is quoted at considerable length, because it shows very clearly the mode of reasoning adopted by the courts at the present day. The judgment is prefaced by a statement of the facts:

That Ferry and May have made contracts like those in question with all the other principal producers of phosphates of the Somme; that the production of all the adherents thus grouped together is about two thirds of the total production of the Somme; that the agreements present the appearance of a contract of commission, but it is not the less evident that they have for their end simply the monopoly [*l'accaparement*] of the product to the profit of the group directed by Ferry and May, and of the two latter themselves, that, in fact, each of the adherents must limit his production to a fixed figure; that he is forbidden furthermore to sell or deliver directly, under any form whatever, either in France or abroad, any crude phosphates, dry or milled, of a standard equal to or higher than dry 60 per cent tri-basic calcium phosphate; that a penalty was stipulated in case of infraction of this clause; and that the minimum and maximum selling price was fixed semi-annually in a general meeting, convoked by the order of a supervisory committee.

On the basis of these facts the court reached the preliminary conclusion:

That such agreements are illegal; that they constitute, in fact, a true coalition, tending to advance the course of phosphates above the price which would be fixed by free competition and to prevent sale below the price thus artificially increased; that they fall, therefore, under article 419 of the penal code and would be in consequence null, as contrary to public order.

Certain other facts and considerations, however, were recognized as modifying this conclusion.

Considering that it is necessary, in order that article 419 apply, that there be a union or coalition between the principal holders of the same merchandise or commodity, with the intent of not selling except at a price different from that which would have been fixed by free competition; that it is proper to inquire, if, in the present case, evidence is found of this double fact, both as concerns the union or coalition, and as concerns the end sought or obtained;

Considering, that it is proper, first of all, to observe that the merchandise in question [phosphates] is a product which, be it of the same grade, be it a grade of less richness as to the tri-basic calcium phosphate which it contains, is met with, not only in the Somme, but is further distributed in great quantity over the whole surface of the earth, and notably in various parts of France, Belgium and America; . . .

Considering, on the other hand, that, if it be true that a certain number of the producers of the Somme are grouped around Ferry and May, their common agent, by their adhesion to contracts similar to that of December 26, 1887, it is proper to remember that this group, as results from the explanations furnished at the bar by Cajot & Cie. themselves, represent only two thirds of the total production of the Somme; and that, if it is true, as is observed, that by reason of the geographical situation of the deposits the operations of the said group can have a great importance upon the French market, it is established, on the other hand, that this group is held in check, as well by the outside producers of the Somme, as by other French and foreign producers; . . .

In view of these facts, the court declared that there was not "the union or coalition between the principal holders of the commodity" mentioned in article 419 of the penal code. The court added the following significant statement:

That this syndicate comprises in reality but a part of the phosphate works of the arrondissement of Doullens; that they have agreed upon the determination of the amount of their output, in order to assure the movement to market and principally the exportation of the same, and for the defense of their common interests, and to fight without disadvantage the competition of numerous markets, as well in France as abroad; that one cannot demonstrate in respect to it either monopoly, or attempt at monopoly of the said commodity.

A case of international notoriety, and of some interest on account of the points of law involved, arose in connection with the famous copper corner (1887–1889) engineered by Secrétan in Paris. Appeal was taken to the court of cassation from the judgment of the court of Paris, but the same was affirmed on grounds substantially as follows. Secrétan had caused an advance in the price of copper by his contracts with producers in various parts of the world, who were cognizant of his objects and hoped to profit by his operations, but who had made no agreements with each other. The price of copper, furthermore, was not agreed upon, nor was there any attempt to fix it, though it was hoped and expected that it would be advanced. In considering this situation with respect to article 419 of the penal code, the court of Paris declared that the agreement of Secrétan

as a buyer with the producers as sellers was such as to bring it within the prohibition of the law, as the combinations forbidden by the law did not have to be exclusively among either buyers or sellers, and the agreements of the various producers with Secrétan were in effect, though indirectly, an agreement among the producers. One circumstance, however, essential to the proof of a violation of the law was lacking, namely, an agreement as to the price. From the nature of the arrangement this could only exist in the assumption by Secrétan of an obligation to sell only above a certain price, and no such condition was to be found in the contracts. Hence the court concluded that the law had not been violated.

A rather interesting case came up in 1892 concerning a combination of pottery manufacturers near Grenôble who had established a central selling agency. In view of the facts that the agreement was limited as to time and as to markets, that it embraced only a minority of the producers of the commodity, and that the prices had fluctuated with the market, the court concluded that the agreement was not an unlawful one under article 419.

The courts do not always take this benignant attitude, even at the present day, as may be seen from the next case, which also shows the interpretation put on the law of 1884, regarding *syndicats professionels*, with respect to article 419 of the penal code. Germain-Perret brought a complaint against certain dealers in aërated waters with whom he had been associated, namely, eighteen of the principal dealers of Lyons, who had formed a syndicate in 1891. This syndicate determined the selling price under the sanction of conventional penalties, among which was exclusion from the syndicate, with notice of the fact to the parties who operated the springs, from whom the supplies were obtained, and with whom the dealers had an understanding they should be supplied exclusively. In consequence of the fact that he was no longer a member of the syndicate, Germain-Perret found himself unable to supply himself with mineral waters, except by indirect and more expensive methods. The court said:

Considering that the coalition in question has thus had the effect of advancing the price of waters to him above that which would have been fixed by the natural and free competition of trade . . .

Considering that the right accorded by the law of March 21, 1884, to form syndicates could not exonerate the accused from the responsibility incurred by them by reason of the above facts; that even if the syndicate established by them in 1891 had been within the terms of that law, the exercise of the rights conferred by it cannot render lawful the violation of the prohibitions decreed by articles 419 and 420 of the penal code, which have not been abrogated by that law and are still in force. . . .

An attempt to form a monopoly contrary to article 419 of the penal code was condemned very recently in the case of the St. Astier lime company. This was an association "*sous nom collectif*." The plaintiff, Mallebray, demanded the dissolution of the association, on the ground that it was formed with the sole purpose of suppressing competition among the lime manufacturers of St. Astier. The defendants declared, on the other hand, that it was not an unlawful coalition, such as had formerly existed among them and had been dissolved by judicial decree (December 16, 1890), but a legally organized association. This combination was condemned, nevertheless, on the ground stated in the complaint.

The French civil code contains certain provisions which are of significance with regard to the legality of industrial combinations, namely:

Art. 6. Laws which concern public order and good morals may not be set aside by agreements of individuals.

Art. 1131. An obligation that is groundless or is based on a false ground or on an unlawful ground can have no effect.

Art. 1133. The ground is unlawful when it is prohibited by law or when it is contrary to good morals or to public order.

The provisions of the civil law have often been applied to industrial combinations by the courts, generally in connection with article 419 of the penal code, but sometimes independently where the penal code could have no application. A comparatively early case dealt with an oral agreement of five quarrymen near Liverdun not to deliver stone for the construction of a fort at a price lower than 3.50 francs per cubic meter. The court of Nancy, which tried the case, said that while article 419 of the penal code might not apply, yet this agreement was, neverthe-

less, "contrary to the principles of free competition," and a serious attack on commercial liberty. Hence the court declared it "null and of no effect, as having an unlawful basis."

In the case of the iodine manufacturers (cited above, page 29, in connection with article 419 of the penal code), one ground for the decision was that it was an invalid agreement under article 1133 of the civil code. In the case of the phosphate manufacturers, cited above, page 29, the lawfulness of the agreement was also questioned under the civil law, but the court declared that there was "no condition restrictive of the liberty to sell phosphates which the defendants were eventually engaged to furnish." In the case of the lime manufacturers of St. Astier (cited above, page 33) the lower court had condemned the combination on the ground of article 419 of the penal code; on appeal the case was decided on the border ground of articles 1131 and 1133 of the civil code. The court said, in part:

> Adopting the motives of the first judges; considering, moreover, that is not necessary, in order to pronounce the nullity of the association denounced by Mallebray, to establish that it unites all the conditions exacted for the application of article 419 of the penal code; that it suffices to establish that the obligation of the various parties had an unlawful basis and purpose; that such was the case of the members of the association criticized, since it results from the facts and circumstances of the case that the said association had been formed only in order to forestall and prevent the foundation of Saint Astier of competing factories, which was contrary to the principle of liberty of commerce and industry; that thus the agreement attacked ought to be annulled also by application of articles 1131 and 1133 of the civil code. . . .

In considering the French law and the interpretation of the courts, the first impressions probably would be that they were characterized by uncertainty and inconsistency. It is doubtful, however, if this impression is correct. In the interpretation of the various rules established by the law, it is the effort of the courts, as has been shown by the above citations, to ascertain whether there is a combination exercising a monopoly power in a manner injurious to the consumers. The matter is skillfully summed up by Professor Lévy-Ullmann in a note to a recent

case in the *Journal du Palais*. Professor Lévy-Ullmann chooses to call all industrial combinations "trusts," hence this word is used in the translation.

For the purpose of determining whether the trust submitted to their judgment constitutes or does not constitute a coalition of monopolists united to establish an artificial advance of prices, the judges seek first of all to discover whether the trust represents in the region where it operates the totality, or at least the majority in number and importance, of the producers of the commodity. Further, they take into consideration the area in which the syndicate acts; the more extended the area, the more vast the monopoly and the more difficult its destruction. The duration of the trust agreement furnishes still a third point to be considered. They examine, finally, its influence upon the course of prices; from the balance of prices, before and after the association of the producers; from comparison of these with the results of free competition, is obtained, with a quasi-mathematical precision, the tare of the trust. Number of syndicate members, area of action, terms agreed upon, result as to prices — such is the quadruple determination which is established by the most recent decisions.

Some of the other writers on this subject make a different analysis of the juristic elements of the offense prohibited in article 419. Thus Babled and Colliez agree in stating that the courts recognize the following four elements, viz.: (1) plurality of agents; (2) principal holders of the commodity; (3) a *de facto* change in the price, above or below what would have been effected by free competition; and (4) an agreement not to sell except at such prices. It is true that Babled insists that the courts have erred in holding that there must be an express agreement, and he points out that the text of the law prohibits combinations "tending" to the effects which it desires to prevent. Apart from verbal distinctions, which are of considerable importance in the practical application of the law to this or that industry, etc., there are one or two points that may be noted more particularly. Article 419 furnishes protection against a combination of persons; but a fusion or consolidation, in general, escapes its prohibitions. Babled says that in such case, nevertheless, the parties may be attacked under articles 1131 and 1133 of the civil code, and, indeed, that the courts in case

of need should apply those sections *ex officio*. In France, however, a fusion is an uncommon method of combination. If, on the other hand, the combination is made by establishing a company as a central agency, this, according to De Birague, will not enable the parties who have formed it, and who control it, to escape the law.

Duchaine complains that the law is of little practical value in view of the almost undisturbed monopoly enjoyed by the sugar and oil combinations, and Colliez calls it a "superannuated text," which does not correspond to the necessities of the present day. This writer in fact says that the benevolent attitude of the courts in recent years is "inspired perhaps by the desire to permit the French manufacturers to combat with equal weapons against their foreign competitors."

IV. Conclusion

A comparison of the laws concerning combinations in the three chief commercial states of continental Europe affords a valuable basis for the inductive determination of the proper principles of jurisprudence. It is doubtful whether a study of the whole field would add very much to the solution of the problem. The three countries considered furnish excellent types of three ways in which industrial combinations may be treated. The French law forbids such combinations as conspire to advance prices above a competitive level; the Austrian law declares no criminal penalty against combinations, but by declaring their agreements null and void withdraws from them the protection of the courts; the German law not only does not condemn them, but recognizes their complete validity at the civil law. It is undoubtedly true, as Rundstein says, that, except in America, there is no such thing as a cartell law proper; the laws affect cartells only incidentally.

The tendency is certainly away from penal legislation, showing therein a striking contrast to recent developments in America. In several countries penal laws have been abolished within the last century, *e.g.* in Germany, Austria, Belgium, and Italy. Most of the legislation on this subject to-day dates, however, from a period when combinations had not acquired the signifi-

cance that they now possess. The only really noteworthy attempts at new legislation respecting industrial combinations have been made in Austria, and it is significant that the Austrian cartell bill of 1897–1898 (cited above, page 26) did not contemplate their destruction, but their recognition and subjection to governmental supervision. A somewhat different attitude, it is true, was taken in the recently introduced bill, concerning the relations of the sugar-beet growers to the manufacturers. This bill provided that all *rayon* cartells, or agreements on the part of the manufacturers to divide the field, should be null and void, as well as all boycotting agreements on the part of the beet-growers; and it also provided penalties for those who should attempt to put such agreements into effect by intimidation or force. This is a return in the policy of the government to the principles established under the prevailing system of law.

Positive conclusions with regard to the merits of these different systems cannot be attained by analysis of the laws alone. A very extensive knowledge of the social and economic conditions and of the practical working of the laws is equally necessary, but for this the data obtainable are as inadequate as the subject is elusive. It is an easy and obvious criticism that, whether combinations are liable to criminal penalties, as in France, or to a declaration of nullity at the civil law, as in Austria, or have full validity, as in Germany, they flourish in all three countries. The vital question is whether combinations are as inimical to the public welfare in one country as in another, and to what extent the legal system may account for such differences as may exist in this respect. In this connection, also, it would be proper to study the powers and vigilance of the public administration in preventing abuses. These subjects are beyond the scope of the present inquiry, but proper information on these points might considerably alter conclusions drawn from the laws.

According to the French law industrial combinations *per se* are not prohibited, but only combinations which commit certain acts held to be injurious to the welfare of the community. An indiscriminate prohibition, in the face of powerful economic tendencies supported by widespread if not general consciousness in business circles that these tendencies are economically

necessary and defensible, fails almost entirely in achieving its purpose. It overleaps the bounds of justice and expediency. It condemns the loose combination, while giving complete validity to the fusion. It condemns the good and the bad combination, without effectually restraining either of them. If the law aims to destroy monopoly, the loose combination is no more guilty than the consolidation. Monopoly, however, is practically recognized and established by the state in many ways. It is idle, therefore, to say that monopoly is wrong and must be extirpated whenever and wherever found; monopoly is a fact which often exists of necessity and which the law cannot destroy. The injurious element which has made both combination and monopoly odious is extortion, but this is not a necessary element of either of them.

It is the recognition of this fact that is the great merit of the French law. The French penal code, in prohibiting combinations tending to give a commodity a price other than that which would be fixed by free competition, aims to check and punish extortion, and that is a perfectly proper matter for criminal legislation, whether it is considered from the standpoint of jurisprudence or of political economy. The form of the law is doubtless crude and antiquated, but it has been saved by the skillful interpretation of the courts. It has one great fault, namely, that it is applicable only to a combination of persons. The evils which it seeks to punish, however, may be committed, and in these days of "trusts" are likely to be committed, by a combination of persons which the law does not recognize as such — by a combination which the law regards as a single person, viz., a corporation. This danger is not so great in France as elsewhere, but it forms nevertheless a theoretical defect in the law. In France the cartell organization is preferred to the consolidation, and if the law can be applied, as recent cases seem to indicate, to the central company (*comptoir*, *syndicat*) of a cartell, this objection to a large extent disappears.

In a similar manner the civil law of France recognizes the legality of combinations, provided their acts are not injurious to the public welfare according to the standard of free industry. This seems to be a much fairer and much wiser system than to declare them invalid without respect to their character or opera-

tion. Herein the French law, or rather the law as it is interpreted by the French courts, seems superior to the Austrian law as that is interpreted by the Austrian courts. It is true that the Austrian law declares that the agreements of a combination are null and void only in case they aim to raise the price of a commodity to the disadvantage of the public, but the courts have taken the position that this is a necessary result of such a combination, and that the question of the actual course of prices is irrelevant. As the law thereby withholds its protection from all combination agreements, whether harmless or injurious, it tends to degrade the former, and gives an opportunity to the unscrupulous to repudiate their engagements.

The German law does not make this mistake; it puts a cartell contract on the same basis as any other contract. The good cartells are allowed to pursue the even tenor of their ways, the bad cartells are subjected to the various penalties and disabilities provided for all persons and associations under the criminal and civil law. In this respect, indeed, there seems room for improvement in more complete protection against cartell excesses, particularly against arbitrary treatment in the supply of commodities and against the demand of extortionate prices.

The prohibition of extortion through excessive prices is not to be confounded with the legislative regulation of prices. Legislation fixing a "just price" is sometimes practicable and desirable, but it is not adapted to many branches of industry. While legislative regulation of prices is impossible as a general remedy, it seems none the less certain that the *crux* of the whole problem is the prevention of extortionate prices and not the prohibition of combination. If the price extortion of a combination is not destroyed by the competition it excites, it will not be destroyed by legislation against combination. It is easy to consolidate ownership. Where strong "natural monopoly" elements exist, competition is quite sure to be eliminated in the long run. The relief which is sought for the evils attributed to combinations may be obtained more effectively by directing attention to prices, and the remedies available are to be found, not only in the law, but also in administration and in public enterprise.

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XXI

THE NEW COMPANIES ACT, 1900[1]

THE wickedness of the company promoter is no new thing: in the wild bubble craze of 1715 one gentleman proposed to float a bubble, or company, to import jackasses from Spain, and another a company for a purpose "to be disclosed hereafter," and decamped in the evening with his pocket full of guineas; but at the same time it is the adoption of the principle of limited liability which has given the company promoter his great opportunity. That principle is now so familiar that it is difficult to realize how modern it is — in fact, not yet fifty years old. Since 1862, when previous tentative experiments of Parliament were reconsidered and embodied in the Code Napoleon of the limited company, there have been numerous amending Acts, but it is only within the last six or seven years that public opinion, of the city prince no less than of the country parson, has demanded radical reform.

The late Lord Chief Justice brought before the public in 1898 some startling figures.[2] During the seven years from 1891 to 1897, 28 millions of money was lost, 20 odd to shareholders, and 7 to creditors. These figures, though much quoted, require very considerable correction, for they are at the same time too comprehensive, and not comprehensive enough; on the one hand Lord Russell took no account of the losses made by companies wound up voluntarily and not under the jurisdiction of the Court, and if these be added, the average *annual* loss for the five years ending December, 1897, works out at 12 millions of money at

[1] From the *Economic Journal*, Vol. XI, 1901, pp. 180–192. The substance of this paper was delivered as a lecture at the London Chamber of Commerce, the President, W. Sandeman, Esq., in the Chair, on Wednesday, Nov. 21, 1900.

[2] See *Times*, Nov. 10, 1898.

the least.[1] On the other hand, the whole basis on which these figures of assumed loss are calculated is unsound; for much of the apparent loss of capital on winding up is compensated by schemes of subsequent reconstruction or amalgamation.[2]

The law allows, no doubt, far greater freedom in England than is possible abroad; anything, for instance, like the "simultaneous formation" usually employed in Germany, where the promoters *must* themselves take all the shares, would not be tolerated here for a moment; and many have felt there is a grave danger in sacrificing any portion of this freedom.

"Restrictive provisions which may have the effect of either curtailing the facilities for the formation of companies which bring so much business to England, or of embarrassing the administration of companies, or deterring the best class of men from becoming Directors, are not to be lightly entertained." [3]

In 1894 a Department Committee presided over by Lord Davey was appointed and reported in 1895:[4] the Committee received memoranda from many Chambers of Commerce and other public bodies throughout the United Kingdom, and took evidence as to the law of companies in France, Germany and America, and may be said to have brought within the four corners of a blue book every suggestion that the wit of man has ever heard, thought or dreamt of in connection with Company Law Reform. The Committee at the end of their report submitted a draft bill of 49 clauses: this Bill was examined by a committee of the House of Lords in 1897, and two following years, and was finally introduced into Parliament by the Secre-

[1] Eighth General Annual Report by the Board of Trade in companies winding up in 1899, p. 6; see also return of Joint Stock Companies, August, 1899, pp. 326–329.

[2] This the Board of Trade officials are the first to admit; see Eighth General Annual Report, *sup. cit.*, p. 6. How much apparent loss is so made good the Board of Trade Report says it is impossible to estimate.

[3] Report of Lord Davey's Committee, 1895, p. vi. Evidence was produced before that committee that the paid-up capital of companies in England amounted in 1894 to 1035 millions sterling, of companies in France to 420 millions, and of German companies to 300 millions, giving a surplus to English companies over the other two countries of 315 millions.

[4] The committee consisted of thirteen names, all of the highest authority in the world of commerce and law, amongst them, Lord Justice Vaughan Williams, Mr Justice Buckley, Mr. Palmer, Mr. John Hollams and Sir Albert Rollit.

tary to the Board of Trade last summer and passed into law: every clause in the Bill has been tossed to and fro a hundred times; outworks against roguery skilfully run up by Mr. Palmer one day were swept away by the flood of Mr. Justice Buckley's caustic criticisms the next: every line of the Bill has been swamped in a flood of discussion and printers' ink : it is sad that after such a lengthy period of incubation the legislative chicken has emerged so imperfectly shaped.

The result of all this discussion has of course been a compromise, and the original 49 sections have now shrunk to 36. The discussions on the Bill revealed general agreement as to the more serious mischief to be remedied, and it is worth while to enumerate the prominent ones.

1. *The One Man Company.* — In order to secure registration with limited liability the Act of 1862 requires the signatures of seven[1] persons to the original memorandum of incorporation, each taking one share in the company, but up to the present English law has taken no heed whether those seven signatories are dummies or no; that company may be really constituted by one man who pays the first subscription for each of the other six, and so secures their signatures.[2]

2. *Insufficient Subscription.* — Many companies proceed to

[1] In Germany, since 1892, limited liability partnerships — Gesellschaften mit beschrankter Haftung — may exist. American law, of course, varies: in the state of New Jersey "three or more persons may become a corporation" (*i.e.* a company), Revision of 1896, Sec. 6: three also are sufficient for incorporation in the state of New York, Law of 1890, Sec. 2: Lord Justice Lindley advocated that one person should be allowed the privileges of incorporation provided he wrote *Limited* after his name.

[2] This is the result of the decision of the House of Lords in Aron Solomon's case in 1896. Solomon floated off his business as a leather merchant into a company consisting of himself, and his wife and daughter and four sons, from whom he received in payment £20,000 in shares, and £10,000 in debentures, with a floating charge over the whole business; he was managing director and could outvote the other six signatories, and by means of his debentures come in with priority in a winding up over ordinary creditors; when the inevitable winding up came the liquidator tried to get the whole set aside as futile in law and fraudulent in fact, that it was no company, but one man attempting to evade the ordinary law of bankruptcy and trade with limited liability by means of six dummies. Mr. Justice Vaughan Williams and the Court of Appeal sympathized with the liquidator, but the House of Lords held that the Act was satisfied with actual signatories whatever their motives.

allotment, though totally insufficient capital has been subscribed. English law, from 1862 up till January 1, 1901, has required neither a minimum amount per each share nor a minimum amount of shares to be subscribed before the company can proceed with its business.[1]

The Registrar of joint stock companies quotes a curious case which illustrates the absolute absence of restraint in these respects prior to the present Act; in 1891 "The Ancient Gold Fields of Africa, Limited" was registered with a capital of £10,000, divided into 9,600,000 shares of one farthing each; the total subscribed capital according to the last return was $1\frac{3}{4}d.$, *i.e.* precisely one share for each of the original seven signatories. It is obvious that a company which starts on its career with too little working capital is as much foredoomed to failure as a school without scholars.

3. *Overloading the Purchase-price.*—The law regards directors and promoters as trustees for the shareholders of the property of the company, but the difficulties of securing disclosures have always made evasions easy, and of these overloading the purchase-price was one of the commonest: in the normal course a promoter finds a flourishing industrial concern worth, say, £10,000, and decides to float it as a company for as much more as he can get; he obtains from the proprietors a contract or option to sell for £10,000; he then forms a small syndicate which is registered as a company, and purports to sell to it the contract or option at an enhanced price, say, £50,000; the syndicate next sells to the person who is to appear before the public as the vendor of the business, again, of course, with an advance;

[1] Abroad limits are usually fixed in both cases. As to the amount of the share this was in France originally required to be at least 100 francs, but in 1893 this limit was reduced to 25 francs, so as to encourage the small investors; in Germany the lowest amount per share is usually £50, though £10 shares are allowed in exceptional cases (1895 Report, p. 15). In America, New York requires shares to be not less than five, or more than one hundred dollars (law of 1890, Sec. 2, 4). As to amount of capital subscribed, in France, by the law of 1893, the whole capital must be subscribed and one-quarter paid up, and the same rule holds good in Germany. New York requires at least five hundred dollars with which to begin business (Sec. 4), and one-half of the whole capital stock to be paid up within a year (Sec. 5). New Jersey requires a minimum of one thousand dollars with which to commence business (Sec. 8, iv).

probably by this time we have got to £100,000; and lastly, the nominal vendor purports to make what is called a provisional contract with another dummy called the trustee for the company, subject to adoption by the company; by this time we are in the region of high finance, and the price may be anything up to seven figures. The promoters thus keep piling up profits on each transaction, and the so-called contract with the syndicate, with the nominal vendor, and the provisional contract with the trustee for the company are obviously not real contracts, all these persons being the nominees of the promoters.

4. *The Prospectus.* — It was generally felt that much more might be legitimately required of the prospectus than was secured by the old law; that all the material facts connected with the promotion of the company should be stated, and the directors forced to sign, so as to pin them down to legal liability for all statements in the prospectus.

5. *Registration of Debentures.* —The whole machinery of debentures (*i.e.* generally mortgages issued by the company of all its property) is beset with difficulty; the common course nowadays is for the new-born company to issue both shares and debentures together, and for the vendor to take the debentures in payment and so keep his grip on the neck of the company. Take a case mentioned in the last Board of Trade Report in winding up, of the Savoy Press, Limited, where an undischarged bankrupt formed a company to purchase from himself a worthless publishing business which he had been carrying on for twelve months previously; the price was £1500 paid to him in cash, shares and debentures; the company ran for two and one-half years, incurred debts up to £600 to ordinary creditors, then the vendor came in, ousted the company, and resumed possession by his mortgage as debenture holder.

What makes a company debenture such a powerful instrument is that the law allows to the company what it does not to the private trader, viz., the power to mortgage the whole undertaking as a going concern, by what is known as a *floating charge* in the debenture. This does not affect the property of the company so long as the latter is solvent, and the company can freely deal with the property, sell, replace and even mortgage the

stock-in-trade, and so on; but directly the debenture holder proceeds to realize his security, the charge floats no longer, but attaches with limpet-like tenacity to all the property the company has at the moment. The Courts have so favored the floating charge that they even allow it now to attach to uncalled capital, though this result was not arrived at without a struggle,[1] and Lord Justice Romer[2] and others expressed strong opinions in favor of restricting floating charges so as not to attach to uncalled capital.

The Act of 1862 required each company to keep a register of mortgages, to be open to creditors and shareholders, but not to the general public. This provision, however, has long been a dead letter, for the Courts held that a mortgage was equally valid between the parties whether registered in the company register or not.

Lord Davey's Committee decided that in view of the peculiar advantages enjoyed by companies the law demanded amendment, and that a public register should be required, open to inspection by every one, to contain those particular kinds of mortgages or charges, with regard to which companies enjoyed a privileged position.

6. Lastly, there was much discussion about the rights and duties of auditors. Auditors are not valuers,[3] and must take much information at second hand, but the shareholders are entitled to believe they have some assurance that the company is sound if the balance sheet is signed by a competent firm of auditors. Proposals were made that balance sheets should be filed annually, and be open to public inspection, but this was resisted in the interests of both public and private companies.

[1] In principle this extension appears to be wrong, as it may be in effect to issue shares at a discount, so often declared to be contrary to the principle of the Act: if a company's capital is £100,000 in £1 shares, that, as Mr. Justice Buckley and others were never tired of insisting, should be a reality; supposing all the shares are subscribed for, but only 10*s.* is called up on each share, *i.e.* £50,000 in all. There is then £50,000 still uncalled, and any creditor should he able to rely on that as an asset of the company; yet if debentures with a floating charge are issued, as is usual, at the same time as the shares, the £50,000 uncalled is not really an asset at all; it is mortgaged to the debenture holders and the real capital of the company is only £50,000.

[2] 1897 Committee Report, p. 19.

[3] See Lord Justice Lindley's evidence.

With the one man company, the new Act fails to deal directly, while indirectly the Act considerably strengthens its position. Doubts were suggested by a learned judge in a recent case,[1] whether the certificate of incorporation granted by the Registrar had really created the company, on the ground that some of the original seven signatures to the memorandum were not genuine. Section 1 of the new Act provides that the Registrar's certificate of incorporation shall be "conclusive evidence that all the requisitions of the Companies' Acts in respect of registration, and *of matters precedent and incidental thereto*, have been complied with," so that had Aron Solomon forged the other six signatures to his memorandum, his company would have been all the same duly constituted.[2] Nor does the new Act contain any clauses directly defining the powers and responsibilities of directors and promoters, the clauses in the draft bill on the point being erased,[3] on the ground that the existing law was probably sufficiently stringent to meet all cases of misconduct.[4] Further, some really useful clauses defining the nature of the balance sheet and what it should contain have also been dropped, and there is no doubt that the Act is the weaker for their omission.

The principle of the new Act may be described as "publicity rather than penalty"; to give the death-blow not so much to the fraudulent promoter, as to the ignorant shareholder, in this following the conception of the late Lord Chief Justice.[5]

[1] Mr. Justice Kekewich, in National Debenture Corporation, 1891, ch. 2, p. 37.

[2] A clause in the original draft bill providing that where the certificate of incorporation had been obtained by fraud, this should be a ground of winding up, was cut out in committee.

[3] The proposal was to require of all directors "*reasonable care and diligence*": Lord Justice Lindley was of opinion that these words only reënacted the existing law, Lord Justice Romer thought they went beyond it.

[4] The law, however, is undoubtedly defective in many points, *e.g.* a promoter must make full disclosure to the company of any profits made, that is clear; but what is to happen if he does not? The company can of course have rescission of the contract: but if this be impracticable, the company cannot recover from the promoters their illicit profit; see the very recent case of *In re The Lady Forrest* (*Murchison*) *Goldmine*, *Law Journal*, Feb. 2, 1901, p. 54.

[5] "When appeals are made to the public to subscribe to the capital of undertakings, everything ought to be aboveboard, no concealment, no secret profits."

It is of course obvious that the machinery of the Companies' Acts has been adopted by many entirely private concerns, the managers of which never intend to appeal to the public, or to let any shares go out of the hands of the very small circle of holders, but who for family or business reasons find the principle of limited liability very convenient. Such companies never *mean* to appeal to the public, and most of the evils which the Act was intended to deal with, consequently, cannot in such cases arise, while to impose hampering conditions as to publication of amount of capital or of the holdings of shares and so on, would only be to handicap them in competition with trade rivals. Many witnesses[1] were anxious to draw a hard and fast line between ordinary public companies and private or family concerns. The difficulty of definition, if nothing else, deterred the Committee from attempting such a division, which does to some extent exist on the Continent. But while refusing to draw any clear distinction directly, the Act does, in a half-hearted sort of way, mark a difference between the two classes. Most of the new stringent provisions are to apply only to companies "*which issue an invitation to the public to subscribe.*" These, in fact, are the key-words of the Act, and their definition and application are alike beset with difficulties. Take the definition alone. Must the invitation be a written or printed document, for it seems difficult to "issue" a verbal invitation? And what constitutes an invitation to the public? Would an invitation to all one's friends or to all the members of one's club come within the words? These are questions with which the Courts may be expected soon to be occupied, and the difficulty of applying the phrase will appear directly. Of the provisions of the act, some apply to all companies, whether incorporated before or since January 1, 1901, and some only to those which are incorporated since that date. To take first the chief provisions applicable:

A. To all companies.

1. In order to check the evils of proceeding to allotment with insufficient capital subscribed, which have already been alluded to, the act imposes two new restrictions: on every application for a share, the applicant must pay a sum not less than five

[1] *E.g.* Lord Justice Vaughan Williams and Mr. Sinclair.

per cent of the nominal amount of the share (Sec. 4 (3)), and further, on the occasion of the first allotment by a company, the act requires for the first time a definite amount of money to be paid into the company's coffers before allotment, viz. either the whole amount of the shares offered to the public; or else, if the company has definitely fixed in its memorandum or articles, a certain amount less than the whole issue on which the directors may proceed to allotment, then that amount. If the amount subscribed does not comply with one or other of these conditions then the directors will be personally liable, after forty-eight days, to see that the money is repaid to the applicant, and any waiver by the applicant of the rules is expressly forbidden.[1]

Section 4 generally deals only with share capital, and with such capital when "offered to the public for subscription." As a further precaution, every company limited by shares is within one month of allotment to file a return with the Registrar of Joint Stock Companies, stating the amount of shares allotted, and the names and addresses of the allottees (Sec. 7): if any of the shares are allotted for services rendered, *e.g.* to a solicitor or vendor, and not for cash, the contract under which such shares are allotted, stating their amount and the services or consideration for which they have been given, must also be filed;[2] this contract will then be open to inspection by intending shareholders: this clause is in substitution for a similar and much discussed provision of the Act of 1867,[3] and is meant to secure the shareholders full knowledge as to the terms on which all shares have been allotted. Curiously enough this Section 7 as to allotment returns, applies to all share companies, public or private, and whether they have issued an invitation to the public to subscribe or not.

2. The third and fourth evils to be dealt with were overloading the purchase-price and the prospectus; and it is mainly through alterations in the law as to the latter that full disclosure is secured as to the former. The prospectus is defined as any "notice, circular, advertisement or other invitation, offering to the public for subscription or purchase any shares or debentures of a company," — not a very satisfactory definition: it would be

[1] Section 4, (3), (4), (5). [2] Section 7, 1, b. [3] Section 25.

comparatively easy to frame a document which would secure all the purpose of a prospectus, *i.e.* advertise the company and the fact that it was doing business and prepared to sell its shares without definitely "offering" them to "the public for subscription." But assuming a document within that definition, then Sections 9 and 10 apply a great variety of new rules to it: it is to be dated, signed by each director and filed with the Registrar (Sec. 9). The prospectus must further contain a great many features, which it is impossible to set out in anything like detail; it must state the contents of the memorandum, the number of founder's shares, and of qualification shares for directors, the minimum subscription on which the directors may proceed to allotment, together with particulars as to shares or debentures issued for considerations other than money. Then come several provisions to prevent overloading the purchase-price: the names and addresses of all vendors of property purchased by that company must appear, together with the amount payable in cash or shares to the vendor, and where there have been a *succession of vendors, then the amount paid to each;* the amount payable for good will (a frequent excuse for concealed fraud) is to be set out particularly: the sum paid as commission for procuring subscriptions, for preliminary expenses, and generally anything paid to the promoter, must also be clearly specified, and finally the dates and parties to every material contract entered into during the previous three years, not being a contract made in the ordinary course of business, must be set out, together with the place where such contracts may be inspected. In the bill as originally drawn disclosure was required of "every material contract and every material fact," but on the energetic protest of Mr. Palmer and others in committee these very wide words were somewhat narrowed and defined. With regard to second or subsequent prospectuses, if issued to the outside public (and not to members only), these provisions apply with modifications. Where published in a newspaper, too, the act takes pity on the pockets of the company and permits the requirements to be somewhat reduced, *e.g.* the contents of the memorandum may be omitted (Sec. 10, § 6). The act is silent as to the penalty if these rules are disobeyed: for any one, *e.g.* a

director, *wilfully* violating the act in this respect, the penalty is probably that of a misdemeanor, with two years' imprisonment under Section 28; and any purchaser of shares, injured by non-compliance, will have an action for damages against the person liable, though he probably will not be able to secure rescission of his contract with the company.[1] But it is specially provided that a director can escape liability by showing that he was not aware of the facts, which should have been disclosed and were not (Sec. 10, § 7). The act supplements, it does not abrogate, the liability of the company or directors under the old law. Owing to the definition of a prospectus the new rules can only apply to companies which appeal to the public.

3. The fifth difficulty mentioned above was the insufficient registration of debentures: and Section 14 provides that, without interfering with the old register (though that, as we saw, was practically disused), a new register is to be kept by the Registrar of Joint Stock Companies, open to public inspection (Sec. 14, § 8), and a copy of the new register is also to be kept at the companies' offices: in this register must be inserted (not all mortgages, note, nor even all debentures), but (a) *any mortgage or charge to secure debentures:* this refers to the usual covering deed to secure debentures, but would probably also include the registration of debentures containing charges in themselves and unaccompanied by any covering deed: (b) *a mortgage or charge on uncalled capital:* the act does not go so far as Lord Justice Romer proposed and abolish such mortgages altogether: (c) *a mortgage or charge created or evidenced by an instrument which if executed by an individual would be a bill of sale:* it is impossible here to venture into the quagmire of the Bills of Sale Acts, but the general result of this clause is that every mortgage or charge of "personal chattels" as defined by those acts must be registered, if the mortgage or charge is such as to give the mortgagee or chargee the power to take possession of the chattels: "personal chattels" under the Bills of Sale Acts do not include stocks and shares: this subsection will not therefore compel mortgages by deposit of shares with a bank to be registered: (d) *a floating charge on the whole undertaking or property of the company.*

[1] Cf., for similar difficulty, Companies' Act, 1837, Section 38, now repealed by Section 33 of the 1900 Act.

The old law, as we saw, rendered the old register useless by allowing validity to mortgages though not registered: the present act closes up this hole of escape by providing that in the above four cases the mortgage or charge unless registered within twenty-one days shall be void as against liquidators and creditors.

4. The last difficulty mentioned was the definition of the duties of the *auditor*. The provisions of the original bill on the subject have been much cut down, at the same time Sections 21, 22, 23 are useful, and a great improvement on the old law. Every company, whether public or private, whether appealing to the world for subscriptions or not, must have an auditor, properly remunerated: if an auditor is not appointed at the annual general meeting the Board of Trade may themselves appoint (Sec. 21): when appointed the auditors are to have full right of access to the company's books and the right to demand all necessary information; they are to sign the balance sheet and to add a certificate definitely stating whether their requirements as auditors have been complied with, and also whether in their view the balance sheet exhibits a true and correct view of the state of the company's affairs. It is curious to note that the act does not in terms say there is to be a balance sheet, only that the auditor is to sign it, presumably if there is one: it is very doubtful if the Courts will treat this as impliedly requiring a balance sheet in every case.

B. 1. With regard to regulations applicable only to companies incorporated since January 1, 1901, there are new rules laid down as to directors' qualification shares; the act does not insist on such a qualification, but says that, where the articles of the company require it, in order to avoid difficulties which arose, under the existing law, either the director must sign the memorandum for the amount of these shares or (if not an original director) sign and file with the Registrar a definite contract to take the proper number of shares from the company and pay for them (Sec. 2, ii); the section does not say explicitly with whom the contract is to be entered into, whether with the company or not. In any case these requirements are only necessary in the case of companies which "issue an invitation to the public to subscribe," a phrase which again causes difficulty. What is to

happen if a company, established on a private basis, and so managed for two years, then requires more capital and appeals to the public? Will the original appointment of directors become void because these rules were not observed? The act gives no answer to the question though the Courts will probably soon be called on to do so.

2. As already mentioned, the idea of a double registration (preliminary and final), of a company, common on the Continent, has not met with favor here, and Lord Davey's Committee reported against it. At the same time the act indirectly does adopt something of the sort by enacting in Section 6, that no company shall in future "commence business" until certain things have been done. This requirement will in no way affect the registration, but, unless and until the requirements of the section are complied with, the company though registered and in existence will be in suspense; it cannot make binding contracts nor borrow money. The preliminaries which must be complied with before business may be commenced are: (i) the proper amount of shares must have been allotted (*i.e.* either the whole amount offered or the proportion required by the articles, Sec. 4); (ii) the directors must have paid a required proportion of their qualification shares; and (iii) the secretary must have filed a statutory declaration that these rules have been complied with. The Registrar will then issue a certificate allowing the company to commence its business. This section again only applies to companies which "issue an invitation to the public to subscribe." A private company need not get the certificate to commence; but how are people, who wish to contract with a company, to know whether it is within the terms of this section or not? Whether it has appealed to the public or not? The point is important, for if it is a private company which has not gone to the public, then any person contracting with the company will be safe and the company will be bound, but otherwise, if the company has appealed to the public and not got the Registrar's certificate the company will not be bound by the contract.

3. Though these many restrictions are imposed on those companies which appeal to the public to subscribe, they are allowed one compensating privilege, viz. that in their case under-

writing is in future to be legal, and the long recognized custom of the City at length receives the sanction of the Legislature, but only on these express terms, viz. that the payment of the commission and the amount of rate per cent are authorized by the articles and disclosed by the prospectus[1] (Section 8).

Finally comes the question: Will the act achieve its purpose and check fraud? That it will provide work for the courts for years to come is clear. The drafting is not good and the difficulties of interpretation, some of which have been pointed out, are numerous. But criticisms of the act go deeper than that: the provisions as to the register of mortgages, the prospectus and the duties of auditors are all useful and should give some protection to the public, but as it is proverbially easy to drive a coach and four through Acts of Parliament, it should be easy to drive one through or at any rate round some of the chief provisions of this act: there is more than one way of circumventing the "commencement of business" provision, of which much is clearly expected; for instance, the company may in its articles mention some merely trifling sum on which to proceed to allotment, or if the promoters shirk the publicity of this course, they can simply start in a very small way, with seven members, all directors, a small capital of perhaps £100, issue this all nominally to the public, and so secure the Registrar's certificate; they could then at once launch out, increase their capital, say to £500,000 and proceed as at present.

Again, all the restrictions on companies which issue an invitation to the public can at one stroke be rendered futile: many companies domiciled near the Stock Exchange never appeal directly to the public at all; they are "baby creations," owing their birth to strong promoting parents, their shares are dealt in more or less artificially by the parent company, public quotations of the shares appear, and eventually the public rush in and buy: the effect of these clauses will probably be largely to encourage this underground process.

In a word, considering all the time spent upon it it is a pity that the act achieves so little.

MONTAGUE BARLOW

[1] This clause has already received judicial interpretation. See *Burrows* v. *Matabele Gold Reef, Ltd., Sol. Jo.*, 1901, p. 378.

XXII

THE PROMOTION OF COMPANIES AND THE VALUATION OF ASSETS ACCORDING TO GERMAN LAW[1]

GERMAN Company Law was entirely changed and recast by a statute passed in 1884, which introduced a number of checks and restrictions of an entirely novel character. Many fears were expressed at the time. All enterprise was to be hampered in the future and driven to foreign countries. No persons of means and standing were to be found who would incur the liabilities and risks to which directors and promoters were to be subject under the new state of things. Sufficient time has now elapsed to show that the forecast of these prophets of evil was based on misapprehension. The statistics prove conclusively that the formation of new companies, far from being arrested by the greater stringency of the law, has been progressing in a most remarkable manner, and that the career of German companies has, on the whole, been most prosperous.[2] Some of the new

[1] From the *Economic Journal*, Vol. X, 1900, pp. 1–19. See Ring, Aktiengesetz, 2d ed., Berlin, 1892; Pinner, Das Deutsche Aktienrecht, Berlin, 1899; Esser, Die Aktiengesellschaft, Berlin, 1899; Riesser, Die Neuerungen im Deutschen Aktienrecht, Berlin, 1899.

[2] There were in Germany in 1896 according to Professor R. van der Borght's estimate (Conrad's Handwörterbuch, Vol. I, 2d ed., pp. 192–194) 3712 companies limited by shares with a total paid-up capital of over £340,000,000, and with reserve funds amounting all together to £58,000,000; the annual net earnings of 3249 companies amounted to about £32,400,000, or about 10 per cent of the paid-up capital. It is safe to assume from the figures given that not less than one-half of the total number of these companies were formed after the Act of 1884. In the blue book published by the departmental committee of the Board of Trade in 1895 (7779) a letter is quoted from Mr. Gerb of the British Consulate General at Berlin estimating the total paid-up capital at £200,000,000 (see p. 29). I showed at the time (see p. 30) that the capital must be at least £300,000,000, and the statistics given in the text prove conclusively that Mr. Gerb's estimate was still further from the truth than I suspected.

safeguards have not proved quite as efficient as was expected by the legislature, but the net result has been a clear gain. There are good grounds for saying that dishonest or even reckless company promotion is no longer known in Germany. No doubt commercial and industrious enterprise in that country has lately passed through a period of prosperity, which cannot be expected to continue unchecked; but times of prosperity, as a general rule, facilitate the task of unscrupulous financiers, and the absence of unsound company promotion in such times may be accepted as satisfactory proof of the efficiency of the law.

The statute on stock-exchange and produce-exchange transactions passed by the German Reichstag in 1896, though laying down certain restrictions as to dealings in shares on the stock exchanges, does not touch the law on the formation and management of companies. The imperial commission on whose recommendation that statute was prepared[1] accepted the testimony of experts on all sorts of matters, however remotely connected with the subject of their inquiry, and would no doubt have listened to any complaints that might have been made as to the efficiency of the law of 1884. The fact that no such criticism came forward is good negative evidence of the non-existence of any substantial grounds of dissatisfaction.

Another opportunity for complaints against the efficiency of the Act of 1884 was given by the inquiries of the committee appointed to assist in the revision of the German mercantile code, but in this case also the only points referred to were matters of detail not affecting the main principles of the law. The amendments which were introduced into the new mercantile code in connection with company law are not without importance, but they are all in the direction of strengthening the principles laid down in 1884.

Company law can be looked upon from three different points of view: the shareholders' point of view, the creditors' point of view, and the point of view of the general public. If the shareholders' point of view was the only one to be considered, much might be said in favor of abstention from legislative inter-

[1] The reports and minutes of the sittings of this commission have been published and contain much interesting information.

ference. There is no reason why persons who invest or speculate in the shares of companies incorporated in their own countries should enjoy better protection than those who invest or speculate in the shares of foreign companies, or in other stock-exchange securities. But the two other points of view are of much greater importance; all trading with unlimited liability offers certain safeguards to the creditors and to the general public, which are withdrawn in the case of trading with limited liability, and ought in that case to be replaced by corresponding safeguards of another kind. I mention the general public as distinguished from the creditors, because the dangers to which the general public is exposed by limited-liability trading are of a kind differing entirely from the risks incurred by creditors. Bad company law, as will be explained in the further course of this article, is a direct inducement to the parties concerned to trade in an unsound manner, and the effects of unsound trade, like those of bad sanitation, go very far beyond the area from which it proceeds. There is one principle which should never be disregarded, whenever the privilege of limited liability is conferred by law; the liability of a fund having a fixed and ascertainable value should be substituted for the unlimited liability of individuals. The value of this fund should on the formation of the company correspond with the amount of its nominal capital, and precautions should be taken to prevent, as much as possible, the diminution of this fund during the subsequent stages of the company's existence. Company law should, therefore, find means to assure (*a*) that the value of the property which represents the capital of a company on its formation shall correspond with the amount of the nominal paid-up capital of the company; (*b*) that property of the same value should continue to represent the paid-up capital of the company as long as it is not increased, and that on any increase of the paid-up capital the property representing the increase should be of a value at least equal to the nominal amount of the increase. I shall deal with each set of rules separately.

A.— Provisions as to Valuation of Assets on Formation of Company

The amount of the nominal capital with which a company is started in England is purely arbitrary, and need not stand in any relation to the value of the assets by which it is represented. A trader who converts his business into a company and keeps the shares himself has every inducement to fix the capital at a high figure, and as he is buyer and seller in one person, the price at which the business is sold — apart from the question of stamp duties — is absolutely immaterial.

If the shares are to be taken by the public the character which Company Promotion is apt to assume is shown by the following illustration. A trader wants to sell his business, which is worth £10,000, and approaches a financial agent conversant with such matters. The agent enters into a conditional contract whereby he agrees to buy the business in the event of his being able to form a company with a paid-up capital of £50,000. The price promised under the circumstances would probably be £10,000 in cash and the same amount in shares. The agent then tries to find some financiers willing to form a syndicate for the purpose; if these are found they are substituted as purchasers for the financial agent, who would probably be satisfied with £5000 for his profit on the transaction. These £5000 would probably be divided by him with some friends who helped to collect the members of the syndicate. The syndicate would subsequently sell the business to the newly formed company for the £50,000, and if they succeed in placing the whole of the shares they will, under the abovementioned circumstances, obtain a gross profit of £25,000, but out of this sum some other intermediaries must be paid, legal expenses and stamp duties must be disbursed, and, to judge from recent revelations, the financial press must receive encouragement. The final result of all this is that the company acquires the property at a price representing five times its real value, the difference being divided by a number of people who have all in their way helped to float the company. It is well

known that this rate of profit is by no means exceptional and is frequently exceeded.

Another circumstance has also to be taken into consideration in places in which British Company Law is applied.

Assuming in the case just mentioned, that the public do not take all the shares, the syndicate may consider it worth while to go to allotment on the amount subscribed, and to trust to chance as to placing the rest of the shares at a subsequent period. In the instance given above this would have no effect on the working of the company, as the company would not get any of the proceeds of the shares in any event, but in some cases the purchase price does not absorb the whole of the nominal capital, some portion of the latter being reserved as a working capital; in such a case the company has of course to suffer by the non-success of the issue.

Thus it will be seen that the principle of establishing a definite fund available for the payment of the company's debts, the value of which can easily be ascertained, is in this country departed from in two ways: (1) by the absence of provisions insuring that the property in which the capital is invested in the first instance is taken over at a price representing its true value; (2) by the absence of provisions preventing a company from starting business before the whole of its capital has been subscribed. As regards the second point, the bill which is now before Parliament provides a partial remedy by requiring a statement as to the minimum amount of subscriptions on which the company will proceed to allotment, but this mode of dealing with the matter, though affording a certain amount of protection to subscribers for shares, does not in any way benefit the interests of the creditors or of the general public.

In Germany the genuine nature of the valuation put on the original assets is secured by elaborate provisions which I shall deal with at length, and the starting of business with an insufficiently subscribed capital is prevented by the rules laid down in sections 195 and 200 of the new mercantile code, according to which the corporate existence of a company cannot possibly begin before its whole capital has been subscribed for, and before at least 25 per cent of the amount payable in cash is in the

actual possession of the managers. There are two modes of formation permissible in Germany: (1) the *simultaneous* method, according to which the promoters take up the whole capital and offer it to the public after the formation of the company; (2) the *successive* method, which enables the promoters to offer the shares before the registration of the company; but in either case the subscription of the whole capital must be complete before the company can begin business.

These requirements as to the subscription of the capital would not be of much importance, if the first point to which I have called attention, namely, the adequacy of the value of the property in which the capital is invested, had not been properly attended to. This was done by provisions requiring the following things: (*a*) that certain matters relating to the history of the formation of the company should be inserted into the articles of the company; (*b*) that the promoters should make a report on the promotion transactions, for the accuracy and completeness of which they are civilly and criminally liable; (*c*) by provisions requiring the members of both boards of the company to examine into the circumstances of the formation of the company; (*d*) by provisions requiring an examination by independent auditors in certain cases.

(*a*) The articles have to state (among other things):

(1) The nature of any consideration not being cash against which any shares are issued.

(2) The names of any persons from whom the company on its formation is to acquire any property, and the prices at which any such property is to be acquired.

(3) The total amount of any payments to be made by the company for services rendered in connection with the promotion of the company.

(*b*) In all cases in which any shares are issued for any consideration not being cash, or in which any property is to be acquired on the formation of the company, the promoters have to prepare and sign a written report, in which they have to set out the circumstances from which it appears that the property to be taken over in lieu of cash or to be acquired by the company is worth the amount for which it is to be taken. In this report

all transactions which led up to the ultimate sale of the property in question to the company must be mentioned, together with all prices paid within the preceding two years for the purchase or construction of any part of such property; in the case of a company taking over a whole undertaking the results of the trading of the two preceding years must also be set forth. The term "promoter," according to c. 187, includes all signatories of the articles of association, and also all persons whose shares are not paid up in cash, and section 202 provides that all such promoters are answerable to the company in damages in respect of any inaccuracy or incompleteness in the above-mentioned report; and also that they have to refund to the company any pecuniary benefit conferred by them to any person in connection with the purchase of the property of which no mention is made in the report. Promoters are released from these liabilities if they can prove that the inaccuracy or incompleteness of the report was neither known to them nor could have been known to them if they had applied the diligence of a prudent trader. Third parties who have received any benefit not disclosed in the report are also liable in damages, if the concealment was (or under the circumstances of the case ought to have been) known to them. Any promoter who knowingly makes any false statement in the report in question is also punishable with imprisonment and a maximum fine of 20,000 marks (section 313).

(*c*) Every German company has a supervising board and a managing board; in the case of a "simultaneous" formation the first boards are appointed when the articles of association are signed; in the rare case of a "successive" formation, the general meeting, which has to be held before the registration of the company, has to appoint them. Both these boards have to examine and report on all the circumstances of the formation of the company. They have in particular to inquire into the accuracy and completeness of the statements contained in the promoters' report, and this inquiry must also include the examination of the question, whether the prices at which any property to be taken over by the company are open to any objection (sections 192, 193).

(*d*) In any case in which one of the members of either board is

a promoter or derives any pecuniary benefit from the promotion of the company, and also in any case in which any property is to be taken over by the company on its formation, independent auditors appointed by the local chamber of commerce have to examine and report as well as the two boards and in the same manner. The auditors' report under the law of 1884 had degenerated into a mere formality, but the new code has added some provisions which will make it much more effective in the future.

Under the new law the auditors may ask for any information in connection with the subject of their inquiry which appears relevant to them, and in case of any dispute with the promoters as to the necessity of any such information, the authority by whom the auditors were appointed is entitled to give a binding decision. As long as the promoters decline to give the information, the auditors' report is not issued and the incorporation of the company cannot take place. The remuneration payable to the auditors is not fixed by any person connected with the company, but by the authority by whom they are appointed (section 194). Any agreement to the contrary is void. (Esser, page 24.)

All the reports have to be filed in the registry and are open to public inspection (sections 195, 199). This right of inspection is not taken advantage of to a large extent, but if the reports contained any damaging facts their contents would soon be known to the public and prevent them from taking shares. As mentioned before, the simultaneous method of formation is almost universally applied, and under that method the promoters have to keep the shares and pay up in full, unless the public comes forward. This circumstance alone is a sufficient check against purchases of property at excessive prices.

It is no doubt true that most persons who take shares in new companies are not very watchful in reading reports or inspecting documents, but if there is only one watchful person any irregularity will soon be known in the circles in which shares are usually placed and will damp the enthusiasm, which might otherwise have been created in favor of the new issue.

It may of course still happen that the prices at which property is taken over on the formation of a new company are too high, but the unnatural increase of these prices caused by the com-

missions and profits of middlemen, which is such a characteristic feature of English company promoting, is a practical impossibility under the above-mentioned provisions.

The question naturally arises, How do people in Germany, who take trouble or risk in the formation of a new company, obtain the remuneration, without which they would hardly be inclined to enter into such transactions? The answer is that the profit is entirely derived from the premium at which the shares are sold to the public. It is clear that the profits obtained in this manner cannot be nearly as high as those which are frequently obtained by the English methods of company promotion, but large and adequate profits are frequently obtained, which nobody can object to, as they are perfectly open. The necessity of paying for the shares before they are issued to the public shuts out a certain class of professional company promoters, who may now be said to be non-existent in Germany, but the starving out of this class of men is an advantage from the moral as well as from the economic point of view.

The principal point is this: in England the promoters' and middlemen's profit is added to the nominal capital of a company, whilst in Germany it is added to the price of the shares. To the shareholder it may be a matter of indifference whether he buys shares from the promoters at 100 per cent premium, or whether the company buys its assets at twice their real value and sells him his shares at par, but a creditor is necessarily misled by being told that a company's paid-up capital is £100,000, when the real value of its property is £50,000, the rest consisting of promoters' profits. Moreover, the necessity of paying dividends on a capital swollen by such profits leads to the adoption of unsound methods of trading and bookkeeping.

It has been suggested that the provisions requiring the whole of a company's capital to be taken up before the registration of the company may be evaded by the employment of dummies, in whose names the shares are taken, the real promoters remaining in the background and only pocketing the profit on the sale of the shares in case of such a profit being realized; but such a course does not appear to be adopted in practice, and would, if adopted, in all probability defeat its own object; if the promot-

ers' report was signed by persons willing and able to contemplate their liability with the indifference of the "*vacuus viator,*" the public would not be tempted to take the shares, and the real promoters would lose their chance of a profit.

There are some other possible modes of evasion which have been specially guarded against by the German law.

It is enacted by section 207 that all contracts made within the first two years after the formation of the company for the purchase or construction of any buildings or plant intended to be used permanently for the purposes of the company's business, or of any land or other immovable property at a price exceeding one-tenth of the company's capital, are invalid unless confirmed at a general meeting in a special manner which enables shareholders holding only 26 per cent of the company's capital to defeat the scheme.

A report must be presented to the meeting by the supervising board, which, together with the contract, must, in case of adoption by the meeting, be filed in the mercantile registry. The members of the supervising board are, according to section 208, responsible for the contents of this report in the same way as they are responsible for the original report on the formation of the company.

In the case of an increase of capital, sections 278 and 279 provide for similar safeguards as those existing with regard to the original formation of a company.

B. — Provisions preventing a Diminution of the Property representing a Company's Capital

The measures which are taken for the purpose of assuring that the amount of the original capital of a company is truly represented by the value of its property are insufficient, unless they are accompanied by measures preventing, as far as possible, the diminution of the capital during the subsequent stages of the company's existence. In this respect also the provisions of English law are hopelessly inadequate. The courts have indeed frequently laid down the rule that dividends must not be paid out of capital, but the payment of dividends, notwithstanding

the contemporaneous diminution or depreciation of that part of its property which is called "fixed capital" is considered legitimate and cannot be prevented.

A trust company holding stock, which during the last business year has paid 50 per cent dividend, but before the end of the year became utterly worthless, may include the 50 per cent in its yearly profit, without deducting a penny for the depreciation of the property from which this profit was derived. This is not called paying dividends out of capital.[1] A company, owning a mining lease, may include the proceeds of the minerals extracted in each year in the profit of that year and value the mine at cost price in its balance sheet, although in the course of a few years the mine will be worthless and the lease will have expired. This is not paying dividends out of capital.[2] A company having paid £100,000 for good will and earning an income of £1000 with every prospect of earning nothing, or less than nothing, in the following year, may divide the profit as dividend, whilst the good will is still valued at £100,000. This is not paying dividends out of capital.

The distinction between the depreciation of fixed and circulating capital, which is the basis of these decisions, is unsound from a mercantile point of view.

Income derived from any source, which by furnishing the income becomes gradually exhausted, cannot be wholly considered as income. It is partly income and partly re-payment of capital, like a terminable annuity. There is hardly any property, classed as fixed capital, which is not of a wasting nature. In some cases the wasting process is very slow, in some cases it is very fast, but the rate of waste can be generally calculated with sufficient accuracy to enable a trader to write off the proper amount for depreciation.

If it was really correct to disregard the depreciation of the fixed part of the capital in the calculation of the profits, the total disappearance of such property would not have to be considered either; new buildings and machines would have to be provided and their cost added to the "Buildings and Machinery

[1] *Verner* v. *General, &c., Investment Trust* (1894), 2 Ch. 239.

[2] *Lee* v. *Neuchatel Asphalte Company*, 41 Ch. D. 1.

Account," but the demolished buildings and the disused machinery could still be valued at cost price. In the case of a private partnership such a mode of trading would invariably lead those who adopt it into the bankruptcy court, if it were persisted in for any length of time, but in the case of a private partnership, the fact that retiring partners must from time to time be paid out on the basis of the balance sheet of the last year, acts as an effective check against the overvaluation of permanent investments.

In the case of companies omitting to provide for the waste, new capital must of course be required from time to time, and such new capital may up to a certain point be furnished by a confiding public on the strength of the forced dividends, but the crash will inevitably come some day.

Another objection against the distinction between the two kinds of capital is pointed out by Mr. Palmer (one of the most experienced company lawyers in this country): "It is extremely difficult to determine what is and what is not fixed capital. Thus shares or other assets are sometimes bought by a company without any distinct determination whether they shall be kept or resold . . . further intentions change. Supposing a company formed to buy, sell, hold by way of investment, and deal in shares and that it holds some shares intending at the time to sell, they are circulating capital, but if they happen to fall in price, the company may determine to keep them and thereupon they become fixed capital, and a few months afterwards the company may determine to sell them and thereupon they again become circulating capital." (Company Precedents, Part I, 7th ed., page 540.)

The distinction which the courts have made between circulating and fixed capital and the rule which they have laid down, according to which a company may continue paying dividends notwithstanding the gradual disappearance of its "fixed" capital, have had the further consequence, that the notion of a permanent fund on which the creditors of a limited company can rely, has been entirely abandoned. This was shown in a very recent case,[1] in which it was held that a loss shown on the working of a particular year, for which no reserve is available,

[1] *In re National Bank of Wales* (1899), 2 Ch. 629, 669.

need not be replaced from the profit of the following year. The result of this, translated into bookkeeping language, is, that a debit balance on the profit and loss account may be carried forward as an asset in the balance sheet, and that, whilst this is done, dividends may be divided among the shareholders. By judicious bookkeeping a company may easily arrange to have a profit in each alternate year and a loss in each following year. The loss diminishes the capital, and the profit goes to the shareholders until the capital is exhausted. A law which allows such a state of things turns limited liability into a source of serious public danger. From the point of view of common business prudence the following rules ought to be strictly maintained: a sum representing the depreciation of a company's property, whether acquired for permanent investment or for the purpose of resale, should be deducted from the profits in each year, and either credited to a depreciation account or deducted from the amount at which such property was previously valued. If on the working of a year a loss is shown which cannot be met out of any reserve fund, that loss must be carried forward on profit and loss account, but no dividends can be paid until such debit balance has disappeared from the books.

Some difficulty arises as to the question, What constitutes depreciation? Is it the natural wear and tear and the gradual disappearance of the object only, or is it also the diminution in market or selling value produced by other causes? In this respect the distinction between fixed and circulating capital offers some guidance.

As regards property, such as buildings and machinery, bought or constructed for the purpose of being retained and used for the permanent purposes of the company, the selling value is not really of importance; the durability or usefulness of any such property is not affected by the conditions which affect the price, at which it can be sold, and the company is not any poorer because it is unable to sell such property at cost price; as regards property bought or manufactured for the purpose of being sold or resold, it is of course necessary to consider the market price, which is the only tests of its value. The two classes of property just mentioned do not as a rule exhaust the whole of a company's

property; book debts, which do not belong to either class, are frequently an important item. It is generally recognized in this country that a reduction ought to be made with reference to bad and doubtful debts, but great laxity prevails with reference to debts payable in a foreign paper currency or in a currency based on silver; it is customary for bookkeeping purposes to convert these debts into sterling currency at a fixed rate of exchange, and this fixed rate is sometimes called the "par value" —as if there could be a par value between a metallic currency and a paper currency, or between a gold currency and a silver currency. There is, then, in such cases a tendency to disregard all fluctuations and to retain the old rate of conversion, although it differs materially from the actual rate. In cases where such debts are only of occasional occurrence this is not so important, but in the case of companies whose principal outstandings remain permanently in foreign countries, the consequences may be very serious; an English company having outstandings of a permanent nature in Brazil and converting them into sterling money at the old rate of 24*d*., whilst the present rate is about 8*d*., is doing exactly the same thing as if they valued their outstanding debts at their full value, notwithstanding the fact that two-thirds of the same were known to be absolutely irrecoverable; yet English law seems to allow this system of bookkeeping, and the payment of dividends cannot be prevented, although the company's capital is dwindling away by the depreciation of the currency in which it is invested.

As regards stock-exchange securities bought for permanent investment, it may be somewhat inconsistent to prescribe deductions in respect of loss of market value, but such deductions are prudent, especially in cases where the fall in the market price is due to causes materially affecting their intrinsic value. When, *e.g.*, a stock-exchange security has ceased to pay dividends, it ceases to serve the purpose of investment.

The German law proceeds on the principles for which I have contended in the foregoing observations. Section 261 enacts that (subject to the modifications to which I shall have to refer) the provisions contained in the mercantile code as to the balance sheets of traders generally are to be observed; according to these

provisions all assets and liabilities must be taken at the value, which they had on the date, as from which the balance sheet is made out; debts must be taken at their probable value and irrecoverable debts be written off entirely. The modifications in the case of the balance sheets of companies are the following:

(1) Stock-exchange securities and goods having a stock-exchange or market value must be taken at such stock-exchange or market price, if such stock-exchange or market price is below the cost price; in any other case they are to be taken at cost price.

(2) Other assets are to be taken at a price not exceeding the cost price.

(3) Buildings and plant and other property not intended to be sold or resold, and being used for the permanent purposes of the company's business, may, notwithstanding the fact that their actual value is smaller, be taken at cost price, provided a sufficient amount is written off or placed to a depreciation account, by which the loss by waste or wear and tear is provided for.

(4) Promotion or administration expenses may not be included among the assets.

(5) The amount of the capital and of all reserve and depreciation funds must be included among the liabilities.

(6) The profit or loss resulting from a comparison of the assets with the liabilities must be stated separately at the end of the balance sheet.

It will be noticed from these rules that no asset may be valued above cost price, even in a case where the actual value is above cost price; this provision does not appear very logical at first sight, and it may be urged that it is just as wrong to undervalue the assets as to overvalue them; as regards the latter observation it is obvious that the only persons damaged by an undervaluation are particular classes of shareholders or directors or managers, whose remunerations vary with the profits, whilst an overvaluation, as I have shown above, causes an injury, not only to the solidity of the company and to the interests of its creditors, but also to its competitors and the public generally, through the encouragement which it gives to unsound trading.

There is therefore much more inducement to provide against overvaluation and to disregard the risk of undervaluation which, considering the many temptations in favor of high dividends, operating on the directors and managers of a company, is really not very serious. The illogical nature of the provisions in question cannot be entirely denied, but it was thought prudent that a company should not pay dividends out of unrealized profits, having also regard to the fact that the stock-exchange price or market price is not always quite genuine, and may easily be sent up by fictitious transactions for the very purpose of enabling a company to value securities or goods at a price producing a profit available for the company's dividends.

One of the consequences of the rule, that no asset can be taken above cost price, is that assets which were acquired gratuitously cannot be valued at anything. Some writers have asked, why a company who had received any property by way of gift should not be able to include their value among its assets; but it is hardly worth while to consider this point, as generous benefactors, who give away their savings to trading companies, are freaks of nature which need not trouble the legislator's mind.

A company which acquires the good will of a business for valuable consideration, may value such good will for its balance sheet at cost price, subject to the proper deduction for depreciation, but it cannot value its own good will if nothing was paid for it. (See Ring, pages 46, 602, 613.)

The German code does not lay down any rule as to the manner in which depreciation by wear and tear and waste ought to be calculated. In some cases the natural depreciation is obvious, as in the cases of leases or patents expiring after a certain number of years. The rate of depreciation in the case of buildings, machinery, etc., can also be easily ascertained with the advice of experts; in other cases, common sense and prudence will usually find a way out of the difficulty. As regards good will, depending on personal efforts and qualities, a somewhat rapid rate of depreciation ought to be allowed for; where good will is attached to particular premises, as in the case of inns and hotels, its value is not generally taken as a separate item, but included

in the value of the premises. For these reasons the item of good will is not frequently seen in the balance sheets of German companies.

Another rule of law, which tends to the preservation of the capital of German companies, is contained in section 262, which provides that a reserve is to be formed in the following way: (1) at least one-twentieth part of the net profit of each year is to be credited to this fund, until it shall have reached the tenth part of the company's capital, or such larger part of such capital, as shall be provided in the articles; (2) in addition to this, any net premium realized by the issue of any part of the company's capital must be placed to the reserve fund, as well as (3) any amounts paid by shareholders in consideration of any preferential rights accorded to their shares (unless such payments are used for the purpose of making good any special losses).

The statutory reserve fund cannot be used for the payment of dividends in bad years, but separate reserve funds may be formed for that purpose. (Esser, page 164; Ring, page 631.)

The provisions which I have hitherto discussed are intended to prevent the following mischiefs:

(1) The watering of the original capital.

(2) The dwindling away of the company's assets by the omission of any allowance for their depreciation in the balance sheets.

They cannot, of course, prevent the gradual disappearance of the company's capital by losses in business in cases in which profits cease altogether, but there are provisions which prevent a company from carrying on business after a considerable part of its assets have been lost.

It is provided by section 240:

(1) That if, on the drawing up of any yearly or intermediate balance sheet, it appears that one-half of the company's capital has been lost, the managing board must immediately convene a general meeting, to whom the state of facts has to be submitted.

(2) That in the case of the insolvency of the company, and also in the case of any yearly or intermediate balance sheet, disclosing the fact, that the liabilities of the company exceed its

assets, it is the duty of the managing board to initiate bankruptcy proceedings without delay. A disregard of this provision is punishable with three months' imprisonment and a fine (section 315–2).

There are no similar rules in English law; in the case of insolvency, winding-up proceedings are of course taken as a general rule, but the mere fact that the assets are insufficient to pay its debts, does not prevent a company from continuing business. As long as a company can pay its way by the use of credit or otherwise, so long it can continue to trade in this country; in some lucky cases, this may enable it to retrieve its losses and to start a more prosperous career, but in the larger number of instances, a company, having reached such a low condition, has to procure accommodation on terms so onerous that the chances of profitable trading are very much reduced. The German rule is therefore preferable in the interest of creditors and of the general public.

The German law on stock-exchange transactions passed in 1896 has no such wide purposes as the above-quoted sections of the mercantile code relating to companies; its only object was to hinder certain kinds of stock-exchange speculations; in so far as it deals with shares in companies, it refers not merely to shares in German companies, but to shares generally, nor does it refer to all dealings in such shares, but only to dealings on any authorized stock exchange. In England the stock exchanges can at their discretion make rules as to the conditions, under which a settlement or quotation is granted to any shares or debentures or other securities, and this was also the case in Germany prior to 1896, but since the statute of that date, the stock-exchange rules are partly fixed by law. The provisions in question have therefore no direct connection with company law, but as they have to be considered on the formation of a company, whose shares are to be dealt in on the stock exchanges, and also on any increase of its capital, some reference must be made to them.

The rules in question prescribe:

(1) The compulsory issue of a prospectus, the authors of which are under a specially stringent liability;

(2) The lapse of a space of time between the incorporation of the company and the public issue of its shares;

(3) The fixing of a minimum capital for companies whose shares are to be dealt in on any stock exchange.

As regards the issue of a prospectus, it is provided by section 38 of the statute, that before any security is admitted for the purpose of being dealt in and quoted on any stock exchange, a prospectus must be issued, containing all information, which is of any importance for the purpose of ascertaining its true value. German government securities are exempted, and other securities may be exempted by the government of the state in which the application is made, but all shares in companies, whether incorporated in Germany or elsewhere, are included in any case.

It was already provided by the mercantile code, that persons issuing a prospectus by which shares are offered within two years from the incorporation of a company, are liable in damages in respect of inaccuracies or omissions in such prospectus. This liability can be enforced by the company only, whilst the liability imposed by the stock-exchange statute in respect to misstatements in the prospectus can be enforced by any holder of the security to which the prospectus refers. According to section 43 of that statute all persons who have issued or directed the issue of any prospectus containing any inaccurate statement on any matter affecting the value of the security are jointly and separately liable for any loss caused thereby, in so far as they knew, or ought in the absence of gross carelessness to have known, that the statement was incorrect. In the same way they are liable in respect of omissions as to essential facts, if caused by them knowingly or recklessly. If the inaccuracy or incompleteness was known to the claimant at the time of the purchase, or ought to have been known to him, on the application of the care usually given to his own affairs, he loses his claim to damages or restitution.

As regards the interval of time which must elapse before a company's shares can be dealt in on a German stock exchange, it is provided by section 39 that the shares of any undertaking which has been converted into a company cannot be admitted

among the securities negotiable on any German stock exchange, unless at least a year has elapsed from the date of the registration of the company, and unless the first yearly balance sheet of the company has been published together with the profit and loss account. Power is given to the state government of the place in which the shares are to be dealt in, to dispense from this rule in exceptional cases. It will be noticed that this close time is only prescribed in the case of companies taking over an existing business; the shares of a company starting a new business may be publicly dealt in at once. The wisdom of the rule is very doubtful. A company cannot be registered before its capital is fully subscribed. The promoters must therefore hold the whole of the shares for at least a year and probably some months longer, as in most cases some time will elapse after the end of the year before the balance sheet can be drawn up and published; some compensation must, of course, be sought for the prolongation of the risk and capital outlay, and this compensation has, of course, to be paid by the public. On the other hand the safeguard is purely imaginary. By judicious manipulation profits belonging to a former year or to the subsequent year may be squeezed into the critical twelve months, so as to produce a specially good profit and loss account, and the idea that the public in this way have an opportunity to see the working of the undertaking before they are asked to subscribe to it is therefore purely imaginary.

The third regulation introduced by the stock-exchange statute is intended to prevent stock-exchange transactions in the shares of companies having a small capital only. The fixing of the minimum capital for each stock exchange is left to the federal council by section 42, which section also gives power to the same body to make further regulation for the admission of securities to any stock exchange.

An order was issued by the federal council pursuant to this power, containing the following provisions:

(1) The minimum capital of companies whose shares are to be dealt in at Berlin, Hamburg or Frankfort must be £50,000, whilst for all other stock exchanges a minimum capital of £25,000 is fixed.

(2) The prospectus must state (*a*) the name of the company, (*b*) the clause in the articles or resolution authorizing the issue, (*c*) the purposes for which the proceeds of the issue are to be applied, (*d*) the amount of the total issue, the amount offered, and the amount retained, and the time during which the last-named amount is to be retained by the promoters.

The provisions about statements in prospectuses and dealings on the stock exchanges are of minor importance and affect a limited class only; those relating to the prevention of over-capitalization and the preservation of capital affect the whole trade of the country. It is stated on good authority that some branches of trade (such as the cycle industry) are rapidly going down in England owing to the fact that they are worked by overcapitalized companies. This will show that the reform of company law has other objects than the protection of careless persons against unsound investments. If this fact could be understood and realized by public opinion, it would be seen that measures like those proposed in the bill which is now before Parliament touch the real mischief as little as the previous voluminous legislation on the subject.

ERNEST SCHUSTER

XXIII

THE GERMAN POTASH SYNDICATE: A TYPICAL KARTELL[1]

I. Introductory

THE actual source of the world's potash supply is at present in the deposits of potash salts found in northern Germany. The great Stassfurt potash industry is based on the presence of those salts in the so-called Magdeburg-Halberstadt rock salt basin. Smaller and commercially unimportant are the deposits of the same type found in Galicia, Chili, Persia, and Eastern Asia. Germany thus possesses a practically complete monopoly of potash salts. Their solubility and the ease with which they can be converted into concentrated products are the qualities which have made the world envious of Germany's possession of this great resource.

The story of the discovery and development of these deposits is interesting. For hundreds of years salt springs had attracted attention in the Stassfurt region. At length, after a number of unsuccessful attempts in the decade 1850 to 1860, rock salt was discovered after penetrating several strata of peculiar bitter salts. The salts designated "Abraumsalze" were regarded as worthless, — an obstruction to the mining of rock salt. Professor Marchand showed that they contained certain valuable elements, whereupon the Prussian government started to sink a shaft in 1858 for the purpose of mining them. Small quantities of the crude salts were subjected to a process of concentration and sold for industrial uses. The success which attended the opening of the Prussian mine induced the Grand Duchy of Anhalt to open a second one, which began operations in 1862. But the value of the "Abraumsalze" was immensely enhanced when, after a series

[1] *Quarterly Journal of Economics*, XXIII, 1913, pp. 140 *ff.* I am indebted to Professor Tosdal for additions and emendations bringing the subject to date. Copious footnote references, except for such new material as is added to the original, have been omitted from this scholarly piece of work on account of space. — Ed.

of painstaking investigations, Dr. Frank, assisted by Justus von Liebig, demonstrated their value for fertilizing purposes. These discoveries inaugurated a new era for the Stassfurt industry, which now, by reason of its lower cost of production, possessed a great advantage over other sources of potash. The price of muriate of potash, which ranged from $75 to $100 per metric ton in 1862, fell to one-third that price in 1864 and 1865.

At present only the potash salts with the highest potash content are mined. Of these, the most important are carnallite, kainite, hard salts, and sylvin. Carnallite is a hydrated double salt of muriate of potash and magnesium chloride, used especially as the basic salt for concentration into muriate of potash. Kainite is also a double salt containing potash in the form of sulphates and chlorides of potash mixed with sulphates and chlorides of magnesium. It is more valuable than carnallite and can be used directly as a fertilizer. Hard salts are a mixture of kieserite and kainite with sylvin. Sylvin is the most valuable of all the crude salts. Like hard salts it finds its chief employment in industry, while kainite is used chiefly in agriculture.

In the export trade the concentrated salts play a much more important part than the crude salts. Muriate of potash (KCl) is the most important, being used in immense quantities as a fertilizer for sugar beet, cotton, and other crops. Sulphate of potash (K_4SO_2) is manufactured in smaller quantities, of which a large part is absorbed by tobacco culture in the United States. Such potash products as carbonate of potash, manure salts, and the crude salts, bergkieserit, sylvinite, schönite, are of less importance.

The annual output of the German potash industry shows an extraordinary increase during the past half century, as is indicated by the following table:

OUTPUT OF POTASH SALTS

	In 1000 Metric Tons	Value in 1000 Marks
1862	19.8	340
1870	291.9	2,628
1880	665.9	6,783
1890	1274.9	16,500
1900	3050.6	39,111
1905	5043.5	60,391
1909	7042.0	81,655

The production of muriate of potash also shows large increases. A significant change in the demand appears in the fact that, whereas in 1861 no potash was sold for agricultural purposes, by 1880 agriculture took 42.5 per cent of the total output and in 1905, 84.5 per cent. Although the consumption of potash in the glass, soap, and other industries has increased in absolute amounts from year to year, it forms relatively a steadily diminishing portion.

The United States is the largest consumer of potash outside of Germany itself. The increase in the importation of potash during the past twenty-five years has been marked. Owing to the frequent changes in classification it is difficult to obtain a comparable set of figures; but for muriate of potash, the most important of the products imported, the increase since 1884 has been nearly tenfold. Sulphate of potash and manure salts show a slower but still significant growth. Nevertheless, the American consumption per acre of tillable land is as yet only one eighth of the consumption in Germany. Three fourths of the potash imported into the United States is used in the Atlantic and South Central states, in the form of commercial fertilizer, of which potash is a constituent.

The potash trade in the United States is handled by the New York agency of the potash syndicate. Several groups of buyers may be distinguished. First, the powerful fertilizer manufacturing corporations, of which the largest are the American Agricultural Chemical Company, of New York, and the Virginia-Carolina Chemical Company, of Richmond, both organized in the late nineties as combinations of existing fertilizer concerns. To these was added, in 1909, the International Agricultural Corporation, a result of the developments of 1906–1909, which led the so-called independents to combine. The Virginia company owns a controlling interest in the Einigkeit potash mine in Germany, while up to the end of 1912, the International owned the Sollstedt mine. A second group of potash buyers is formed by the large packing houses, which buy potash for their fertilizer plants, and the smaller independent fertilizer manufacturers. Finally there are manufacturers of chemicals, dry mixers and jobbers of fertilizer, farmers' associations, and local dealers.

II. Early Agreements. The First Syndicate (1889–1898)

Following the entry of the two fiscal potash mines into the field of potash production, the factories established by private individuals for the manufacture and concentration of the crude salts began in 1864 and 1865 to outstrip the capacity of the market to absorb their products. The number of enterprises had increased from three in 1862, to eleven in 1863 and eighteen in 1865. Commercial depression and overproduction resulted in the failure of nearly a third of the companies in the latter year. Rapid recovery and subsequent prosperity again brought about, in 1871 and 1872, an increase of manufacturing facilities not warranted by demand. The decline in the price of muriate of potash which began in 1872, and lasted until in 1874, put a number of factories out of business. The pressure toward some sort of combination led to an agreement between the manufacturers in 1876, whereby prices were to be fixed weekly by a commission. With the resumption of prosperity in the following year, several of the members withdrew and the agreement came to an end.

In contrast, the development of the potash mines up to 1875 was one of steady progress. But in that year, a third mine at Westeregeln, and a fourth, New-Stassfurt, in 1877, deprived the fiscal mines of Prussia and Anhalt of their monopoly in the production of crude salts. In view of the fact that any one of the four mines could, if necessary, supply the total demand, the fiscal mines did not relish the idea of unrestrained competition. The expected happened. The alternative of free competition and low prices, sure to entail serious losses upon all of the mines, and eventually ruin to some, was rejected for combination. With the active coöperation of the Prussian fisc, the four mines, Stassfurt (Prussian fisc), Leopoldshall (Anhalt fisc), New-Stassfurt and Westeregeln, agreed to limit for five years the output of carnallite intended for concentration into refined salts. Certain provisions as to the price of crude salts were included, but it was left open to the factories to fix the prices for concentrated products. Between the three kainite-producing mines a similar agreement was concluded in April, 1879, fixing prices and the total amount to be mined by each member.

The success of the potash mines was an incentive to the investment of capital in new enterprises of the same sort. A mine at Aschersleben began operations in 1882, and threatened to rob those already in the field of their market. Westeregeln's notice in June, 1883, of withdrawal from the carnallite agreement led to its dissolution in October. However, after some negotiation efforts at securing a new agreement were successful, and on October 21, 1883, representatives of the five mines signed contracts renewing the previous one. As the Aschersleben mine also produced kainite, the necessary revision of the kainite agreement was made and Aschersleben became a member in 1884.

At the time a seventh mine, Hercynia at Vienenburg, became a party to the carnallite agreement, several changes were made. Special privileges, that of fixing the price of crude salts sold to the factories, and the right to veto a reduction or increase in allotments, were conceded to the Prussian government. The price-fixing privilege was of small importance except to the fiscal mines, since the private mines supplied only their own factories operated in connection with the mines.

Shortly after the renewal of the carnallite agreement in 1883, the manufacturers of muriate of potash formed an association for marketing concentrated products. As the supply of raw material was fixed by the mine owners, no restriction of production was necessary. The organization, somewhat more elaborate than in previous agreements, provided for a central sales office through which all the manufacturers agreed to market their products. The manager of the sales office, acting according to instructions formulated by a representative commission of manufacturers, effected sales, received orders, and assigned them to the members as nearly as possible in proportion to the quantities of raw material assigned to them by the mine owners' association. Occasional excesses or deficits were to be adjusted semi-annually. The commission fixed the price of muriate of potash, but could raise it only with the consent of the Prussian fisc.

The potash industry prospered during the decade following the formation of the first agreement. The combination, including as it did all the producers, had been able to keep up prices

and, at the same time, increase the demand for potash. The addition of three new mines had not been a disturbing factor. The advantages of regulation had become too evident to allow a return of free competition upon the expiration of existing agreements. Strengthened by observation of the results of competition which had taken place between the pooled and independent muriate factories in the American market, the opinion became prevalent that a renewal of existing contracts was insufficient and that all products, crude and refined, should be included in a new and firmer agreement. Finally there was formed, during September and October, 1888, the first all-embracing potash Kartell or syndicate, upon the basis of seven separate contracts or agreements, the first four of which related to crude salts, the last three to refined products.

The members of the syndicate proper were mine owners exclusively. Owners of special factories (*i.e.* factories not operated in connection with any particular mine) who were members of the muriate agreement of 1883 were compelled to observe the conditions prescribed in the last three contracts as to the production and sale of concentrated products. In return, they were assured an exclusive supply of raw material for the greater part of the syndicate's duration of ten years, with the warning that they would be cut off from all supplies if they were found to encourage the establishment of a new potash mine. The output of the special factories had been steadily decreasing, and when the Prussian fisc, which had operated no factory of its own, withdrew formally from the existing agreements to establish a factory in 1887, the business of the special factories had decreased to such an extent that they offered to pay the Anhalt fisc higher than current prices in order to secure crude salts. Consequently in 1888, the assurance of raw material was welcome to them.

The first two of the seven contracts (designated I*a* and II*a*) dealt with carnallite. A commission of representatives from the seven mines fixed the total amount to be mined and allotted it by percentage shares to the individual mines. Minor provisions regulated the raising and lowering of quotas. Kainite containing 12.4 per cent pure potash was chosen as a basis for the calculation of allotments. The kainite contracts (II*a* and II*b*) dealt

similarly with the allotment of production, but since kainite, unlike carnallite, is sold in its crude state for agricultural purposes, its sale was placed in the charge of a central sales office, the producers agreeing to make no independent sales, to observe the terms of sale fixed by the central office, and to make regular and accurate reports. Selling prices were fixed by a committee of the associated mine owners, subject, however, to certain privileges conceded to the Prussian Minister of Commerce and Industry. He was given the right to name special prices for the supply used in domestic agriculture, whenever it should seem advisable in order to increase sales, or necessary for the welfare of German agriculture. The detailed provisions for the temporary transfer of allotments during disturbances in operation need not be mentioned here.

The last three contracts (I*c*, I*d*, II*c*) had substantially the same aim as the others, — the elimination of competition and the prevention of overproduction. The special factories, together with the factories of the mine owners, were all subjected to the restrictions of a central sales agency, the orders being assigned and adjustments made as under former agreements. Prices and rebates were fixed by a general commission, which was also empowered to dispose of quantities of muriate of potash, at specially low prices, or gratis, for propaganda purposes to chemists for experiment, for exhibitions, for the support of agricultural trade papers and the like. This was the beginning of a type of endeavor which has been most effective.

Since the administration of each of the basic agreements was in the charge of a separate committee, the management proved so unwieldy as to necessitate a reorganization in 1891. A centralized administration was introduced. The general management, of which the representative of the Prussian fisal mine was *ex officio* chairman, obtained broader powers; while a general commission, consisting of one representative from each mine, performed the duties of the several committees under the old arrangement, fixing prices, deciding important questions of organization and distribution, and imposing penalties for breach of contract. The general or business management was divided into three departments, each headed by an assistant director. One

of these took charge of the domestic business and the transactions between the syndicate and the individual mines; another took the export trade; and the third, the statistical work and the propaganda movement. As before, orders were received and assigned and adjustments made at the central offices. The syndicate, which now styled itself "Verkaufssyndikat zu Leopoldshall-Stassfurt," established agencies in several German and foreign cities, while in others it gave certain dealers exclusive control. Up to 1893, the American trade had been controlled by two exclusive dealers, but the syndicate's dissatisfaction with the growth of the American demand under their direction led to the establishment of a special agency in New York.

During this syndicate period (1888–1898) five new mines became members of the syndicate. The fever of speculation from 1895 to 1898 did not pass the potash industry by. It is said that over a hundred boring companies were in operation and many shafts were sunk. The failure of not a few companies, and the depression at the close of the decade, led to the abandonment of many of the enterprises. But in general the syndicate succeeded in increasing the sales of potash and in steadying the market. Though it was not able to avoid overproduction entirely during the difficult years, 1892–1893, it prevented the industry from experiencing the worst effects. On the ground that the existing facilities were too large, the Prussian government advocated a restriction upon the establishment of new mines. The policy of restriction did not appeal to the legislature at that time. The debate on the 18th and 19th of April, 1894, in the Abgeordnetenhaus, was concerned chiefly with the question of whether or not the Prussian fisc would have influence enough, should restriction be adopted, to secure lower prices for domestic industry and agriculture; it ended with the rejection of a proposed law.

III. The Second and Third Syndicates (1898–1904)

As might be expected, little opposition developed when the question of the continuance of the syndicate came up for decision in 1898. The agreement of that year differed from the

preceding one in that a single comprehensive contract took the place of seven. The products were divided into four groups according to their potash content. The management of the syndicate was given greater freedom and authority by the adoption of the stock company form. Instead of a commission consisting of a representative from each mine, a supervisory council of fewer members was created. During the three-year existence of the second syndicate, five mines were added to the membership.

Again, in 1901, renewal of the syndicate upon substantially the same basis as in 1898 was effected without difficulty. The opposition which was manifested concerned mainly the question of the admission of new mines into the syndicate. It was becoming apparent that the number of mines was increasing more rapidly than it was possible for the syndicate to increase sales.

After 1901, however, the situation became serious. The depression of 1901 and 1902 resulted in a decrease of the syndicate's business, the effects of which were accentuated by the entrance of new mines. From seven mines in 1888 and twelve in 1898, the number of producing mines had risen to twenty-four in 1902 and twenty-eight in 1903. The necessity of bringing all these into the syndicate, the unwillingness of the older mines to give up any part of their allotments in order to make room for new members, and the high demands of prospective members rendered the allocation of quotas a progressively difficult task. The market from 1902 to 1904 was unsettled. Both dealers and consumers delayed buying, toward the last, in the hope of obtaining lower prices in the event of the dissolution of the syndicate.

IV. The Syndicate of 1904–1909

Early in 1903, dealings of American potash purchasers with some of the newer mines which had not yet entered the syndicate gave rise to rumors, very disturbing to Germans, that the Americans intended to buy up potash properties and supply their own demands. The subsequent entry of these mines into

the syndicate quieted the fears for a short time, only to be again aroused by the report that the Virginia-Carolina Chemical Company was attempting through the Heldburg Company to obtain control of the Wintershall mine, in addition to its ownership of a controlling interest in the Einigkeit mine. Though this report was denounced as false it caused much resentment. It was said that the loss of the American market, which amounted to one half of the total export trade, would be a calamity to the industry as well as lead to wanton dissipation of the natural resource.

At the instance of the Prussian fisc, negotiations aiming at the continuance of the syndicate, which expired in 1904, were taken up early, the first general meeting being called for May 8, 1903. This early action, hastened it is said by the reports of the American "invasion," recognized that the renewal would not be effected as easily as on previous occasions. Although the syndicate included all the operating mines (after the entrance of the mines Hohenfels, Kaiserroda, Einigkeit, and Bleicheroda, in January, 1903) this complete control was of short duration. Moreover the internal composition of the syndicate had been undergoing a change by the division of the members into two hostile groups, one composed of the older mines having comparatively large quotas and unwilling to submit to the decreases attendant upon the increase of syndicate membership, and the other made up of newer mines demanding larger quotas in some proportion to their alleged capacities. According to a clause in the existing agreement, syndicate members were free after June 30, 1904, if renewal had not been accomplished by that date, to execute independent contracts for delivery after December 31, 1904. Consequently, all efforts were directed toward effecting a renewal by July 1, 1904, in order to avoid the complications which would inevitably arise should independent contracts be made.

At the general meeting, May 8, 1903, it was voted that the continuance of the syndicate was desirable and that the invasion of American capital must by all means be prevented. Two committees were chosen, one to discuss the draft of a new agreement, the other to take up the allotment question. Fol-

lowing the admission of three new mines into the syndicate, the general meeting on November 3 took up the discussion of the proposed basis for renewal. It was soon discovered that the chief point of dispute was the allotment question. A special committee, instructed to report at the next general meeting, was chosen to attempt to induce the various mines to agree to a compromise table of divisions. The committee found it impossible to accomplish anything. No less than eighteen out of twenty-eight mines raised objections to a table of allotments submitted for inspection in November.

The second general meeting of syndicate members on January 18, 1904, showed a sharp division on the allotment question between the two groups of mines. The group of older mines declared it would not submit to any further reduction of allotments and demanded that the younger mines agree among themselves as to the division of the balance of the total output. The latter elected a committee to consider the matter, but the high demands of certain mines precluded a settlement. Two general meetings, February 8 and 29, did not alter the state of affairs. After the mine Burbach gave formal notice of its intended withdrawal, some of the mines were deprived of the hope they had entertained that the agreement would be renewed according to a provision inserted in the contract that, should no member give notice of withdrawal before June 30, renewal would automatically take place. Nevertheless the deadlock continued, each side accusing the other of a shameful display of selfishness.

Finally on June 27, a meeting called by the Prussian fisc convened in a sort of fatalistic hope that efforts would be successful. By June 30 minor questions had been disposed of and one by one the mines agreed to quotas assigned to them by a special commission. The government mines finally agreed to make concessions, but the obstinacy of the representative of the Hedwigsburg mine brought the negotiations on that day to naught. The mine owners were brought together the next day; Hedwigsburg expressed willingness to enter the syndicate upon the somewhat more favorable terms offered. Hohenfels had, in the interim, contracted with several American firms to deliver potash at prices considerably lower than those quoted by the syndicate.

This was adjusted, the syndicate assuming the contracts, and upon July first, the new syndicate was organized.

Upon August 11, the new syndicate (Kalisyndikat, G. m. b. H.) was entered in the commercial register at Bernburg as a limited liability company with a paid-up capital stock of 400,000 marks entirely owned by the members of the syndicate. The adoption of the company form, merely a device to give juristic personality to the Kartell, was due to the desire to secure still firmer organization than had hitherto been possible. Potash products were regrouped into five groups, the first three of which included certain crude, mixed, and concentrated salts, the other two, crude salts. As before, members of the syndicate bound themselves to place the entire output of their establishments at the disposition of the central office which received and distributed orders. To increase the effectiveness of the syndicate's propaganda work, all individual trade marks were given up.

The administration of the syndicate was intrusted to three bodies: the general assembly (Generalversammlung) consisting of a representative from each mine; the supervisory council (Aufsichtsrat); and the syndicate management (Syndikatsvorstand). The general assembly was empowered to choose eight members of the council, to declare dividends, to determine the terms of sale, and, with some qualification, to amend the articles of the company. Any change in the prices of certain products, as well as any change affecting the privileges of the Prussian Minister of Commerce, required the votes of the government representatives to be among those concurring. Upon the supervisory council, of which the chairman was to be chosen by the Prussian Minister of Commerce and Industry, devolved the duty of selecting the officials composing the business management, and of exercising control over them. The syndicate managing staff (Geschäftsvorstand) consisted of a Generaldirektor, with three subordinate directors each in charge of one of the three departments into which the business was divided: namely, the central department, the agricultural bureau, and the business management proper, which again fell into four divisions dealing with (*a*) crude salts, (*b*) concentrated products, (*c*) American

trade, (*d*) transportation. The Vorstand fixed prices annually, subject to the approval of the supervisory committee, upon the basis of kainite containing 12.4 per cent pure potash, the other prices being computed therefrom according to potash content. Export prices were to be higher for all except a few products with low potash content, — an exception of little importance since such products cannot be economically transported. By other provisions, the approval of the Prussian Minister of Commerce was made necessary for raising the base price. The right to quote special prices for German agricultural consumption was retained.

An arbitration board was established for the settlement of disputes. Penalties for breach of contract took the form of fines ranging in amount from 100 to 300,000 marks. Appeal from the decision of the supervisory council was permitted. As security for the observance of contracts, each mine, except the fiscal establishments, was required to deposit 300,000 marks to the credit of the syndicate.

The fatal weakness of the syndicate contract lay in the fact that in it were incorporated no provisions for the admission of new members. In the anxiety lest the syndicate should not be continued, a most important question was glossed over and finally left unsettled. This defect was destined to cause constant difficulties.

The period of calm which followed the formation of the syndicate in 1904 was of short duration. The establishment of new mines, their increasing reluctance to enter the syndicate, and the difficulties and disturbance accompanying become the main features in the history of the potash industry. The syndicate led a precarious existence, threatened with destruction more than once in the course of the protracted negotiations connected with the entrance of certain mines into the organization.

When possible, the syndicate secured the assent of a prospective member to a provisional agreement and assigned a quota tentatively. Then began a process of higgling, the new mine demanding a high quota with the hope of obtaining eventually about what was desired, and occasionally enforcing its demands by threatening, or actually making, independent sales at

low prices. The syndicate, on the other hand, commenced by offering a low quota with the intention of raising it if necessary. The fact that since 1900 the average output per mine had decreased in absolute amounts each year rendered the allocation of quotas the most difficult problem of syndicate management. From 1900 to 1908, the average output per establishment decreased 41.5 per cent in quantity and 47.8 per cent in value.[1]

The speculation accompanying the revival of prosperity in 1905 found a favorable field in potash enterprises. It was accentuated by the so-called Gamp law passed by the Prussian Diet for the purpose of preventing the multiplication of new mining enterprises. It was provided in this law that for two years from its enactment, no person should have the right to explore for, locate, or secure title to mining rights in the territory where Prussian mining law was binding. As it happened, Prussian mining law did not apply, in respect to potash salts, to Hanover, where all mining rights were the property of the landowner, not, as in Prussia, of the discoverer. Consequently, while the lex Gamp effectually checked potash exploration in Prussia, speculation merely shifted its base of operations to Hanoverian territory. The purchase and sale of mineral rights, the lease of lands, and development on the royalty plan of land bearing potash, or supposed to bear it, furnished great opportunities for the promoter, and the basis for unprecedented potash speculation, and a flood of potash securities of which a gullible public never seemed to get enough. The Gewerkschaft, a form of association in favor for mining enterprises, was, owing to a

[1] Year	Total Output in Millions of Doppelzentners	Total Value in Million Marks	No. of Concerns	Average Output Per Concern	Average Value in Marks
1900	30.4	56.2	15	202,407	3,748,688
1901	34.3	59.1	19	180,604	3,112,027
1902	32.9	56.9	24	137,057	2,370,379
1903	36.6	64.1	28	130,865	2,289,602
1904	43.0	74.1	28	153,621	2,645,634
1905	48.3	81.6	32	151,021	2,551,336
1906	54.8	91.7	36	152,093	2,546,777
1907	55.8	93.4	41	136,092	2,278,587
1908	59.2	97.8	50	118,315	1,956,264

Dr. Kreuzham, in Kartell-Rundschau, 1911. The doppelzentner contains 205 lbs.

peculiarity in Hanoverian law, impossible to organize in that state. Nevertheless, the device of buying up the charters of small or defunct Gewerkschaften in Prussia and other states enabled promoters to circumvent the law, and gave rise to a flourishing trade in charters. Further, the lex Gamp did not affect mining rights already granted. Many enterprises, abandoned after the activity of the years following 1898, became once more objects of public favor and speculation.

It is impossible here to describe the negotiations connected with the admission of the various mines to the syndicate. But the case of Sollstedt, though not typical, is of special interest because of the part played by it in the international complication of later years. In 1905, the Sollstedt mine, owned by H. Schmidtmann, began producing, and made its entrance into the syndicate conditional upon the adoption of certain reforms in the policy of the syndicate, among other things urging the adoption of a lower price basis. Although the opposition claimed that these reform demands were merely a cloak to hide the real demand for a large quota, one cannot deny that a policy of lower prices, in order to remove the incentive to the increase in the number of mines, was entitled to serious consideration.

Unable to secure the assent of the syndicate to his proposals, Schmidtmann closed contracts late in 1905 with several American potash buyers. When it became known that the syndicate was granting larger discounts to the great fertilizer corporations, the Independent Fertilizer Manufacturers Association, consisting of some sixty-five companies, was formed and proceeded to contract with Sollstedt for more potash. In all, the contracts called for the annual delivery of about 50,000 tons of pure potash at prices which, though not specified, were guaranteed to be as low as those currently paid by the large fertilizer corporations. According to the prices paid for potash, American buyers might now have been divided into several groups: first, the two large fertilizer corporations, receiving discounts of eleven and thirteen per cent; next, the group of Sollstedt's customers, some of whom were under obligation to secure their potash from the syndicate up to January 1, 1910 (deliveries to these were not to begin until 1910); other buyers, bound by contract to take their total potash require-

ments from the syndicate at discounts of five and seven per cent; and buyers under no obligations and paying the current prices.

Schmidtmann was much criticized for his action. He was accused of lack of patriotism, of wasting a great natural resource for the benefit of a foreign nation instead of conserving it for the welfare of the German people. Since geological experts estimate the supply of potash salts to be sufficient to supply the world for 600,000 years, the ever-recurring arguments bearing on the subject of exhaustion have little force. The true explanation of the hostile attitude against Schmidtmann and other mine owners who made low price sales to foreign customers, and against foreigners who attempted to buy potash mines, seems to be the belief that the possession of a natural monopoly ought to enable the nation to secure monopoly gains.

At the close of 1905, Sollstedt was more unlikely than ever to enter the syndicate. Toward the end of January, 1906, there was serious talk of dissolving the combination. In the course of the negotiations the syndicate issued an ultimatum, offering quotas to Sollstedt and two other "outsiders," under threat that should the offer not be accepted, steps to effect the dissolution of the organization would immediately be taken. Schmidtmann in answer to this declared that the size of the quota was a minor matter, and that he was mainly concerned with the reforms in organization and in the price policy. No definite action as to dissolution of the syndicate followed. Negotiations were continued. The general meeting of the syndicate refused Schmidtmann's proposal to lower prices, and during the latter part of the year, the Sollstedt conflict, as it came to be known, was allowed to lag. The situation, critical as it was, was aggravated by the syndicate's difficulties with other mines, especially with Deutsche Kaliwerke, which also presented a number of reforms as the condition of its entrance. The crisis became so acute that a number of mines were ready to give notice of withdrawal from the combination as soon as any mine except Sollstedt should sell a single doppelzentner independently. Despairing of inducing Sollstedt to enter, it was proposed to make use of Sollstedt and Schmidtmann's connection with the mine Aschersleben (a member of the syndicate) to bring a suit for damages,

alleged to have been suffered by the syndicate through the connection of the syndicate member, Aschersleben, with the outsider, Sollstedt. Schmidtmann, in his capacity as chairman of the supervisory board of Aschersleben, had carried through several transactions connected with the development of Sollstedt, by the aid of Aschersleben funds; the shares of Sollstedt had been subsequently purchased by Aschersleben. It is unnecessary to go into detail; the upshot of the matter was that a number of stockholders of Aschersleben formed a protective association and attempted to oust Schmidtmann. However, the affair began to clear up, and on May 10, Sollstedt agreed to enter the syndicate, the reform demands being postponed for later discussion and decision. The statement made later in connection with the potash controversy, that pressure of public opinion and fear of government intervention caused Sollstedt finally to enter the syndicate, seems to be only partially supported by fact. Government intervention had been advocated, but for a different purpose, that of checking the increase of new mines, not the regulation of those already in existence.

By the terms of settlement, Sollstedt continued deliveries of potash to its American customers, paying fines for the excess over its allotment. The syndicate was, however, granted the option after January 1, 1908, of assuming the contracts calling for current delivery, while the new syndicate, should one be organized in 1909, was to have the option of assuming all the sixty-five or seventy contracts. The syndicate chose to make use of its option and, upon January 1, 1908, assumed the Sollstedt contracts as binding. Delivery proceeded smoothly for a time, but in June came an unusual influx of orders from the Sollstedt customers, and a corresponding decrease in the orders from those customers of the syndicate who were bound by contract to secure from it their total potash requirements. The officers of the syndicate concluded immediately that the Sollstedt customers intended to resell potash to purchasers already obligated to the syndicate, — a conclusion strengthened by complaints of discrimination. The syndicate did not propose to allow any surplus for resale and accordingly restricted deliveries. Sollstedt's American customers protested against this violation

of contract and refused to acknowledge the transfer of the contracts to the syndicate. Sollstedt, contrary to contract, resumed independent delivery in July, pointing out that the alleged intended breach of contract on the part of the syndicate's customers did not call for the violation of another agreement, in order to punish the offenders. Owing to the fact that Sollstedt had deposited large security guaranteeing delivery, the Americans could exert considerable pressure. The syndicate accepted the situation without further action at the time.

The trouble with Sollstedt, though the most serious encountered during the existence of the fourth syndicate, by no means stood alone. The mines Rossleben and Ronnenburg which also applied for admission to the syndicate in 1905, settled the quota problem by a compromise and became members in March, 1906. In the same year the Kaliwerk Friedrich Franz entered, in which the government of Mecklenburg was chief stockholder; and the Prussian fisc, in order to strengthen its position in the syndicate, bought the mine Hercynia. The influence of the group of newer mines had been constantly increasing, and at the general assembly in November, 1906, they were able to elect a majority of the supervisory council. They proceeded to make use of their power in an attempt to introduce a reorganization of the syndicate's technical and mercantile policy. This was much facilitated by the change in general directors in February, 1907, following a long dispute and a series of complaints of favoritism to the older mines. But the completion of Sollstedt and the Deutsche Kaliwerke, which threatened the very existence of the syndicate, directed efforts toward inducing these to enter the fold. The agreement with Sollstedt has been mentioned. The set of reforms advocated by the Deutsche Kaliwerke were given up, as in the case of Sollstedt. The question in dispute was finally limited to one of quotas. After appraisal by a special commission and several conferences, the long protracted negotiations came to a close. The syndicate ratified the entrance of Sollstedt and Deutsche Kaliwerke on June 19, 1907. A few months later, in November, three new mines were added to the syndicate membership.

The year 1908 brought no halt to the increase in the facilities for the production of potash. But the older members of the

syndicate were surprised when they heard that a group of capitalists representing the powerful agrarian association, the Bund der Landwirte, had purchased extensive potash properties with the intention of establishing still another potash mine. In view of the distinctly friendly attitude which the syndicate had always shown toward the agrarian associations, it was not to be expected that they would seriously consider competing with the syndicate. The syndicate was successful during the year in inducing all "outsiders" to become members of the organization. At the close of 1908, there were forty-nine mines in operation, all of them syndicate members; sixty-five companies in addition had already begun borings and shafts.

A distinct development of the potash industry in this period was the organization of companies to buy up potash lands in order to prevent the establishment of more mines. Several of the newer mines, headed by the Deutsche Kaliwerke, organized a company (Vereinigungsgesellschaft für Kalibergbau) to buy up potash properties with the express purpose of demanding in return for not developing them, an excess quota from the syndicate, so that reasonable interest on the investment in potash properties could be paid. A group of the older mines also formed a similar association, the Schutzbohrgmeinschaft. Its offer to sell the fields it had acquired to the syndicate was rejected.

The continued overdevelopment of facilities for potash production was due to a complex of causes rather than to any single factor. Various peculiarities of the potash industry have made it a favorite for investment and speculation. The participation of the government in the industry and the patriotic desire to invest in home enterprises doubtless had an influence. But Germany's possession of a natural monopoly and the unusual profitableness of the industry have certainly been prime factors. Dr. Pinner gives interesting figures. In 1906, which he considers a normal year, the average profits of twenty-one mines was 15.9 per cent, while dividends of 13.5 per cent were declared. Within two years the average dividends were decreased to 9.5 per cent, because of the increase in the number of mines and the decreased average output. Upon the basis of expert opinion, Dr. Pinner states that the cost of production of potash

salts varied from 40 to 60 per cent of selling prices. With the smaller average output per mine in 1908, the proportion was somewhat higher, but still low as compared with other mining industries. Potash mine owners do not neglect to make large deductions for amortization and depreciation.

The fact that the capital required for developing a potash mine is considerable seems to have had little effect in checking production. The capital stock of each of the twenty-one mines mentioned above was, with one exception, in excess of $400,000; the average was well over $1,000,000. The average cost of a boring ranges from $15,000 to $25,000, and one at least must be made preliminary to the sinking of a shaft. The risks of the potash industry were insufficient to check investment, although they are of a peculiar nature, especially the danger of water dissolving the salts.

In addition to the unusual profitableness of the industry, one must mention among the inducements to speculation the attempts of the Prussian government to regulate the industry. Reference has been made to the Gamp law. Prominent among the arguments of its proponents was that the passage of such a measure was the only means of preventing potash fields from being monopolized by private individuals. The objection to the law, that a large number of boring companies would be destroyed, was not borne out. Instead, the law greatly increased the value of their holdings. An instance is reported in which the International Boring Company, at Erkelenz, working with a capital of 1,000,000, marks, had acquired a large number of potash fields, and sold them several months after the enactment of the law for 35,000,000 marks. Though the lex Gamp was superseded July 8, 1907, by a new mining law, its provisions were in essentials continued.

The extension of the police requirement that every mine have at least two passable exits was also instrumental in increasing the number of mining companies. The construction of a second shaft necessitated for many mines a large outlay of capital. Since the ordinance could be complied with by connecting two adjoining mines underground, this method was adopted by some of the mines. Other mines holding extensive tracts of land

complied with the law by constructing a second shaft, but, in addition, organized a subsidiary company to take charge of it, and the new company proceeded to demand an independent quota from the syndicate. Among the members of the syndicate which adopted the latter course were Burbach, Westeregeln, Glückauf-Sondershausen, Aschersleben, New-Stassfurt, and Rossleben.

V. The Renewal Negotiations, 1908–1910

Negotiations concerning the renewal of the syndicate began nearly a year and a half before final decision was necessary, — in itself striking evidence that great difficulty was expected. At a general meeting of the syndicate on January 14, it was decided that the supervisory council should submit before May 1 the draft of a new contract. Pending the outcome of the negotiations, the council succeeded in inducing ten mines to refrain from "outside" sales till June 30, 1909. In the hope of strengthening their influence in the syndicate, a number of the mines began to divide their ownings, intending to use the fields controlled by subsidiary companies as defense against the reduction in quota which was bound to come. As an instance, Glückauf-Sonderhausen announced its intention of transferring its reserve fields to six subsidiary Gewerkschaften. The supervisory council proceeded to ask each mine owner to hand in a written statement of his suggestions for reform. In the replies, the evils of the existing situation were evidently recognized by all, but the proposed remedies revealed much divergence of opinion. The propositions of a group of Hanoverian mines, to which ten or eleven mines expressed complete agreement, give some light on the points of controversy. They advocated the creation of a second council (Beirat) to relieve the supervisory council of some of its many duties under the old organization. The duration of the new syndicate should be ten years. The admission of new members was to be left to an arbitration board. Products were to be sold under certified analyses. Transfer of quotas from one mine to another (under restrictions) was to be facilitated. All these propositions, as well as sundry others, were

actively opposed. Transfer of quotas was especially opposed by the fiscal representatives on the ground that it would further the "Vertrustung" of the industry. It would undoubtedly have increased consolidation, and the government's fear of having several less efficient plants shut down, and a number of laborers thrown out of employment thereby, was a chief factor in determining its attitude. Another proposal was that each mine should receive an additional quota for each undeveloped potash field in its possession. The adoption of such a measure would have greatly altered the appearance of the allotment table. For instance, Glückauf-Sondershausen, owning 258 fields, had at the time a smaller quota than another mine with only four.

During the spring and early summer of 1908, the committee of the supervisory council in charge of the renewal negotiations worked constantly to eliminate as much of the friction as possible. The Prussian government had early expressed its opinion that renewal of the syndicate was by all means to be desired; doubt as to the attitude of the fisc was no longer a deterrent factor. It had been stated frankly that should the fisc decline to become a member of a new combination, the chances were overwhelmingly against its formation. The expressed wishes were, as far as possible, embodied in the draft of a new syndicate contract which was submitted to the supervisory council at Eisenach on July 2. According to its provisions, the power of the potash syndicate was to be extended from the sale and purchase of potash to the acquisition of property and other rights. Potash products should be sold according to analyses of their exact chemical content. It was planned to create a second council (Beirat) to assist the supervisory council. The seat of the syndicate was to be changed from Stassfurt to Berlin, — a concession to the younger mine owners, who believed that there the connection between the syndicate and Ministry of Commerce would be more intimate, and that the syndicate would be in closer touch with the great agricultural associations having central offices in Berlin. Of more importance was the proposed freedom to transfer quotas from one mine to another, when owned by the same firm.

The renewal negotiations were in the main a repetition in

intensified form of those in 1903 and 1904. As before, a new agreement must be concluded before June 30 of the year of expiration, in order to avoid the complication of outside sales. The hope of speedy renewal vanished as the months passed, and the entire second half of the year was devoted to discussion of the plan of reorganization; the chief question, that of allotments, was shelved until an agreement on other points should be reached. Among the mass of articles and reports which filled the press, an article of Dr. Wächler, the chairman of Salzdethfurth, one of the older mines, attracted special attention. Pointing out that the syndicate was not in a position to avoid overproduction, he declared that the régime of competition was the only remedy. The elimination of all the less capable companies would place the industry once more on a firm basis. But the opponents of Wächler's view claimed that the excess of mining facilities was the fault of legislation, not of the syndicate, and that price cutting would deprive Germany of all advantage from her natural monopoly. They also stated that free competition would cause enormous losses to a great number of security holders interested in the prosperity of the industry.

When the commission of the syndicate met on January 5, 1909, three sub-committees were chosen, one to deal with the hotly contested question of changing the domicile of the syndicate, a second with the question of the increased utilization of carnallite (urged by the carnallite mines, which felt that their product was not being actively pushed) and a third with the question of the size and transfer of allotments. On April first, a new syndicate plan was published, which left the question of location open, but proposed changes allowing transfer of quotas between the groups of products and between mines. After a discussion by the full commission, and restriction of the right of transfer to suit the Prussian Minister of Commerce, the general assembly, consisting of representatives of all mines belonging to the syndicate, and others about to enter, took up the most difficult problem, the allocation of allotments. It was strongly urged that the old allotment table be taken as a basis and that quotas for the new mines be provided for by a 10 per cent horizontal deduction from the quotas of the older mines, the re-

quired balance to be assigned *pro rata*. But this scheme, as well as others proposed, failed of acceptance, and the allotment question was again referred to a committee, which prepared accordingly a new allotment table, but with as little chance of acceptance as before.

Since there was little doubt that lower prices would follow the dissolution of the syndicate, American potash buyers could hardly be expected to favor its continuance. All the pressure which could be brought to bear on the situation was exerted against the combination. The Virginia-Carolina Company owned 702 of the 1000 shares of Einigkeit, controlling therefore that mine. Nothing substantial appears to have come out of the rumored negotiation between the mine Teutonia and the American Agricultural Chemical Company; the rumor caused a flurry of excitement and the publication of numerous articles under such captions as "Vaterländische oder Amerikanische Bodenschätze?" with repeated patriotic warnings against the invasion of foreign capital. This had the material result some time later of causing such transfers of mining property to foreigners to be dependent on official sanction. That American influence was exerted against the syndicate is shown more distinctly in the transactions concerning Sollstedt and Aschersleben. The chief stockholder, H. Schmidtmann, and his son, W. Schmidtmann, had long been dissatisfied with syndicate management. They wanted to operate at full capacity. The American market was a favorite because of its great capacity to absorb potash, and the high potash content of the wares demanded. Schmidtmann had already secured a huge slice of the American trade by the "outside" sales of Sollstedt in 1905–1906. With some of the American independents he had contracts for delivery up to 1917. Consequently he was not at all averse to the idea of combining the independent buyers. Should such a combination be formed he would contract to furnish potash at low prices. This would please the American potash buyers. Schmidtmann would have long-time contracts for deliveries of potash, and would be intrenched against the revulsion which might follow the dissolution of the syndicate; if renewal were effected, he was in a position to force the syndicate to accede to his demands. How-

ever, the attempt of W. Schmidtmann and C. F. Meadows of Baltimore to organize the Independent Fertilizer Company in the fall of 1908 fell through. A second attempt to combine the independent fertilizer manufacturers in the U. S. Agricultural Corporation, chartered in April, 1909, also bore no result. The third attempt was successful. Between midnight June 30 and daylight July 1, presumably, the International Agricultural Corporation with W. Schmidtmann as president and C. F. Meadows as treasurer came into being, having obtained possession in that same short space of time of the Sollstedt mine, and sold potash which it had bought from Sollstedt. America was, and is, outside of Germany itself, the syndicate's biggest customer. Its influence, exerted at a critical period in the life of the combination, had the inevitable effect of increasing the difficulties of renewal.

In spite of all the complications, it was believed that the syndicate would be renewed at the meetings to be held the last of June. Prospects brightened during that month. Many of the special demands were withdrawn and differences compromised. When the final meeting convened at Berlin, potash buyers from many countries had assembled in the imperial city to await the outcome of the negotiations, the American delegation being conspicuous. Their purpose was clear. In the event of the dissolution of the syndicate a price war would be the probable result, and buyers on the spot would be able to secure cheap potash. The meeting on June 29 was devoted to the discussion of allotments. Negotiations were resumed on the following day. By ten o'clock that evening, thirty-five mines had signified their willingness to enter on the terms offered. At eleven, the Prussian fiscal representative announced that unless there was unanimous agreement by midnight, he would proceed to make independent sales. After a dramatic session, the obstinacy of one mine owner defeated the efforts at renewal. The remaining representatives (of forty-one mines) agreed informally not to make any sales independently until after July 1. On July 1, it was learned that the representatives of the Westeregeln group, the Einigkeit, and the Schmidtmann mines, Aschersleben and Sollstedt, had made large independent sales of potash after leaving the hall at midnight. This added complication pre-

cluded the possibility of organizing a new syndicate on July 1. But the provisional agreement was continued to July 8 and then extended to July 24. In the meantime the German government had threatened to levy an export duty on potash, and the Westeregeln group had succeeded in annulling its "outside" contracts. Upon July 24, a new syndicate was organized, not including Sollstedt, Aschersleben and Einigkeit, — those mines in which American influence was strongest. It was to be located at Stassfurt, and its continuance was contingent upon the satisfactory adjustment by the three outsiders before September 30, of their independent sales. But nothing having been accomplished, a "Kampf-syndikat" was formed without them (on September 30).

Sollstedt, through the International Agricultural Corporation, its owner, proceeded to sell potash to all the independent buyers with whom it had previously contracted, on the same terms as had been granted to the American Agricultural Chemical Company. The total of the contracts (including those of Einigkeit and Aschersleben) involved seven or eight million dollars and called for about 120,000 tons of pure potash, or four fifths of the annual American importation. The contracts, binding for two years, were provided with options on a five-year extension. The unsuccessful attempts of a German commission sent over in August to induce the Americans to give up their valuable contracts, — valuable because the prices quoted were about 30 per cent lower than current syndicate prices. The fact that the syndicate policy of making the export trade pay the largest part of the profits did not operate as nicely when two fifths of the export trade was taken away, the arguments concerning the dissipation of a national resource, the strengthening of foreign nations at the expense of the Fatherland and the like, — all these increased the clamor for legislative interference. As a result, the Prussian government submitted in December a proposed imperial potash law to the Federal Council of the Empire. Though the idea of a direct export tax was given up, the bill proved especially displeasing to the Hanoverian faction; and since it practically nullified American contracts, the opposition which developed caused its withdrawal.

A second committee of the syndicate, which came over to America in December, was as unsuccessful as the first. About this time treaty negotiations in connection with the Payne-Aldrich Tariff were in progress. Following the exchange of a number of informal notes, the United States representing that an export duty would be considered undue discrimination against American trade, the State Department was reported, on January 17, to have received assurances that the German government would not press its scheme of levying an export tax. Germany was soon after accorded the privilege of the minimum tariff.

On February 4, the draft of a new potash law was brought before the Reichstag by the Federal Council. After a lively debate (February 14 and 15, 1910), in the course of which it became clear that the low-price American contracts were at least the occasion of the bill, it was referred to a committee of twenty-eight. Much altered, it came back to the Reichstag and was passed on May 25, 1910, going into force three days later.

The potash law, thus finally enacted, provides for imperial control over the production and selling prices of potash salts until December 31, 1925. The allocation of allotments becomes the duty of the "königliche Verteilungsstelle," a commission of which the chairman and two other members are chosen by the Chancellor, subject, however, to ratification by the Federal Council. The other members are chosen by the mine owners. The Verteilungsstelle estimates a total output sufficient to supply the world's demand, and apportions it among the potash producers. For the same mine, the percentages of domestic and export output must be the same, in order to prevent the possibility of any mine devoting itself exclusively to the export trade. For the current year a scale of prices which should serve as the maximum for domestic and as a minimum for export was embodied in the law. Any potash mine which delivers salts in excess of its legal allotment must pay into the imperial treasury a tax of from ten to eighteen marks for every doppelzentner in excess of its quota. This is in addition to the regular (and almost nominal) tax of sixty pfennige per doppelzentner levied upon the total output of potash, whose proceeds go to

pay the expense of administration of the law, any excess being used for propaganda purposes. The Federal Council is empowered to lower the surtax in the case of contracts executed before December 17, 1909, so that the contract prices plus surtax shall not exceed the prices current before June 30, 1909. For the purpose of checking the increase in the number of producers, the law provides that a new mine shall receive an allotment from the first, but one smaller than its capacity would entitle it to demand. Not until the third year shall full allotments be granted. Mines with two shafts shall receive a 10 per cent addition because of the second shaft. Allotments may be transferred between groups of products or transferred or exchanged with other mines, but the transfer of over half an allotment requires official consent.

As an example of social legislation, another provision requires attention. It is provided that whenever a potash mine reduces wages or lengthens the time of employment, its quota is to be reduced by the Verteilungsstelle, on the ground that such action is *prima facie* evidence that capacity has decreased. In the decision, the Verteilungsstelle must call in two labor representatives to act as part of the court. Employees in mines or factories which close because of transfers of allotments are entitled to compensation from the mine owners, up to the amount of twenty-six weeks' pay.

The law provided for no compulsory syndicate. But under the altered conditions which it brought about the Kampfsyndikat of September 30, 1909, was dissolved, and a new one came into existence on June 7, 1910.

VI. The Potash Controversy between Germany and the United States

The potash sold to Americans by the Aschersleben, Sollstedt, and Einigkeit mines was in amount far in excess of their quotas under the new law. The greater part, hence, was subject to the supertax, which nearly equalled the selling prices of the salts. The mines Aschersleben and Sollstedt refused to continue deliveries unless the Americans would assume the tax.

The American holders of low price contracts would not agree to this, since assumption would mean their paying higher prices for potash than those who bought from the syndicate. They denied that the tax was a charge of the nature implied in their contracts, the wording of which was "that any governmental duty should be assumed by the buyers." They maintained it was a penalty for violation of a German law. Expert legal opinion on both sides of the Atlantic split on the question. In Germany the majority held the Americans to be liable for payment of the tax; in America the opposite opinion prevailed. The necessity of securing potash for current requirements forced the Americans to pay the tax, which they did under protest.

Fertilizer interests in this country denounced the law as a practical repudiation of contracts made in good faith, and appealed to the State Department for aid. As soon as the matter could be taken up, in the fall of 1910, it became evident that the Germans did not wish to concede any more ground than was absolutely necessary. The Federal Council refused to consider a reduction of the supertax in the case of the options, according to which the buyers had demanded a five year extension of contracts, in June, 1910. A commercial representative of the State Department, accompanied by a group of fertilizer manufacturers, proceeded to Europe in September. He declared two months later that no settlement could be made; that the application of the maximum clause of the tariff act of 1909 was in order, since the German law clearly was discriminatory against America.

The controversy reached so acute a stage in December that President Taft submitted the whole matter to the Cabinet. Protests of fertilizer manufacturers, of farmers and other potash consumers continued to arrive at the State Department. Upon January 20, 1911, the potash syndicate presented a statement for the consideration of the President and the Secretary of State. The syndicate's brief seems to have been a sober and dignified presentation of the case; though the inclusion of a number of misstatements and assertions insufficiently proved laid it open to attack. But it seemed that the crisis had passed.

The demand of our State Department for a definite statement from the German government elicited a reply which was not made public, but seems to have led to the adoption by our government of the attitude which the German had maintained, namely, that the affair was one to be settled by the parties concerned, and not by international diplomacy. After a series of conferences at Hamburg, an agreement between the Americans (except the International Agricultural Corporation) and the syndicate was reached. Before the controversy could be finally settled, it was necessary to arrange matters with the Aschersleben and Sollstedt mines, which still insisted upon delivering potash subject to the supertax. But negotiations progressed so rapidly that a compromise was soon agreed upon.

The provisions of this final settlement were in brief, (*a*) the withdrawal of all suits in our courts involving liability for the payment of the potash tax levied by Germany; (*b*) the assignment to the syndicate of the American contracts with independent mines; (*c*) new contracts with the syndicate, covering full American potash requirements for five and one half years on a price basis practically the same as that prevailing before the low price contracts were obtained from the independent mines; and (*d*) the reëntry of the independent mines Sollstedt and Aschersleben into the syndicate. Aschersleben bought one half of the Sollstedt shares from the International, and upon January 1, 1911, Sollstedt entered the syndicate. The German government agreed to refund about 60 per cent of the supertax held in escrow in American banks. Aschersleben received 1,050,000 marks from the American Agricultural Chemical Company and the same amount from the International in return for its consent to annul the "low price contracts."

The Einigkeit mine, one of those which made independent sales, was not much involved in the controversy. The low price sales to the Virginia-Carolina Company were insufficient to cover requirements. Forced to buy the balance of its potash from the syndicate, an amicable arrangement was made in 1910, whereby Einigkeit became a member of the syndicate December 31 of that year, paying a sum of about $50,000 to the syndicate as a compensation for "outside" deliveries already made.

VII. The Working of the Potash Law of 1910

The potash law was not wholly a measure concocted on the spur of the moment to deprive American potash buyers of the benefit of their contracts. It is beyond question true that this law, though in its terms not discriminatory against the individuals of any nation, nevertheless in fact discriminated against American purchasers, and was designed to discriminate against them. By its wording the law applied to all German potash mines which produced amounts beyond a certain specified allotment; hence technically it would not appear to be discriminatory. But the American potash purchasers held contracts with the only mines which were liable for the supertax imposed by the law on any production in excess of the specified allotments. Moreover, these contracts had been made in such terms as to render them susceptible of a construction whereby American purchasers would be made liable for the payment of this extremely heavy supertax. In other words, not the owners of the German mines, but the American purchasers from them, were the persons threatened by the measure, and meant to be threatened. Certain it is that the result of this combination of circumstances was decidedly unfavorable to American buyers, and to all intents and purposes amounted to discrimination against them.[1]

But the events of previous years had paved the way for drastic control of the industry. The German government had played a large part in the history of the potash industry from its inception; there had been agitation in 1905 for a state monopoly; previous measures, such as the Gamp law of 1905 and the mining law of 1907, had failed to bring the relief desired for the industry; this bill itself had been under discussion from February until May, 1910, — all these circumstances indicate that the German government had long determined to keep in its hands full control of the industry and of the prices of the products.

[1] Whether the administration of President Taft would have been justified under these circumstances in exercising the retaliatory powers given by the tariff act of 1909 is a question of political expediency upon which I should hesitate to give an opinion, as involving matters which lie outside the economic problems with which the discussion is concerned.

But if the law was successful in preventing low price potash sales, it was in other respects far from being as successful as its originators predicted. Instead of checking the continued increase of new mines, its effect was similar to that of previous attempts at legislation, in furthering the evil it was intended to prevent. As soon as it went into effect a new wave of development began. Not only were vacant fields divided and subdivided to form bases for new enterprises, but the syndicate mines also proceeded to divide their properties to a greater extent than before, founding new subsidiary companies with extra quota demands. Since a concern was legally entitled to a larger quota if two or more shafts were operated, and since, under the law, each new mine was guaranteed a quota, it became necessary for any mine which did not wish to have its quota reduced below a level which would leave a profit, to establish two or three subsidiary companies. Instances are numerous. Aschersleben divided its possessions to form four new enterprises. Out of the original properties of the Gewerkschaft Hugo a full half dozen mines were formed by division. From the Gewerkschaft Amélié eleven new undertakings have been organized, and the list might be continued. With the honorable exception of Prussia, governments have been as great sinners as private enterprises in the promotion of new mines. Anhalt has four and plans two more. In April, 1911, in addition to the sixty-nine syndicate mines, seventy-nine were in process of construction, and about fifty more had either completed or were making borings. A year later, ninety-seven mines were prepared to deliver potash, and a hundred and thirteen were in process of construction. Dr. Paxmann stated in the spring of 1913 that one hundred twenty-seven mines were operating, one hundred thirty-two in construction. The failure of the law in this regard is unmistakable.

The potash law had another effect not desired by its promoters, that of furthering concentration within the industry. The extension of the movement toward concentration which had become a feature of coal mining and banking, was much delayed by the hostile attitude of the syndicate of 1904, — an attitude inspired by the fiscal representatives, opposing transfer of

quotas. Yet the opposition of the syndicate had not been sufficient to keep away concentration entirely. The fear of the loss of influence shared by the fiscal mines, should the private enterprises be free to combine, added little to the deterrent influence. During 1905 certain mines secured control of others by means of stock ownership. Westeregeln, backed by the Mitteldeutsche Kreditbank, acquired three fourths of the shares of the new mine Rossleben. The Schmidtmann mine, Aschersleben, purchased the shares of the mine Sollstedt; and other instances might be given. Yet until 1909, there had been little immediate advantage, except as investment, from the control of one mine by another. Concentration of production was practically prohibited, despite the fact that mines were operated at only a third or quarter of their capacity.

The freedom granted by the potash law in the matter of transferring quotas was a great incentive to concentration. Mines began to buy up quotas or controlling interests in other mines. The Wintershall mine, to which belonged the mines Heringen and Heiligenroda, acquired a majority of the shares of Bismarckshall, and secured control over five other mines. Later it was reported to have obtained control over two subsidiary companies of the Gewerkschaft Amelié. The fusion of the Deutsche Kaliwerke concern and the Amelié was another notable instance. In the next year, 1912, the movement continued, the cases most discussed being the combinations Einigheit-Prinz Adalbert, and Burbach-Krügershall. In nearly every case, the combination of mines was accomplished by means of stock ownership. The purpose was usually at least one of three: (*a*) to save capital outlay in the construction of the second shaft required by the police ordinance; (*b*) to transfer or exchange quotas so as to concentrate production in the best situated mine; (*c*) joint ownership and administration of power plants and branch railroads, or division of risk.

Denunciations of the potash law began six months after its passage and have grown in number and vehemence. The opinion was soon freely expressed that the potash law was a failure; that in order to make a small saving, it had induced speculation and waste of millions. The government finally recognized that

the law had not been operating as intended, in a speech of Minister of Commerce Delbrück. The potash industry became the object of a two days' debate in which a lively discussion as to the employment of the propaganda money was a prominent feature. The tax of sixty pfennigs had yielded a sum much larger than was deemed necessary for propaganda purposes. Proposals to reduce this tax, to allow the excess to go into the imperial treasury, to spend the money more freely, as well as the more important debate on the general ill-success of the law brought about at the time no amendment. Debate was resumed in January of the year 1913, and finally a resolution was adopted to the effect that any reform or amendment to the potash law should be binding for all mines commenced after January 15, 1913. Hanoverian conditions presented some difficulty, but it was generally expected that an amendment or revision of the imperial potash law so as to remedy some of its weaknesses would soon be forthcoming.

Among the definite proposals for the amendment of the potash law, urged in 1913, was one presented by Dr. Paxmann in a memorial to the government in which he advocated a license system according to which a government concession, to be granted only when the demand for potash warranted it, should be required for the opening up of a new mine.[1] In the allotment of quotas, the size of the field was to be made a factor in order to discourage the division of ownings into independent enterprises. An increase in the length of the period during which the new works would not be granted full quotas was also proposed. Hr. Emil Sauer, a prominent potash miner, disagreed with these proposals and demanded the prohibition, until 1924, of new enterprises not already in process of construction.[8]

The year 1913 passed without the publication of the promised amending bill of the government, but finally it was laid before the Bundesrat in February, 1914.[3] The bill was by no means acceptable to potash interests because it seemed to be more concerned with the fiscal interests of the government than with the

[1] K. R., 1913, pp. 199 *et seq.*; Berliner Jahrbücher, 1913, p. 155.
[2] K. R., 1913, p. 215; Berliner Jahrbücher, 1913, p. 156.
[3] Berliner Jahrbücher, 1913, p. 156; K. R. 1914, p. 195.

endeavor to remedy the industrial situation. The chief provisions of the amending bill were (1) the introduction of a direct tax upon potash at a rate which increased with the amount mined; (2) the abolition of the existing tax; (3) the adoption of a new freight basis, Muelhausen; (4) the increase to ten years of the period during which incomplete, provisional quotas were assigned.[1]

Meanwhile, the idea of arresting further overdevelopment of the potash industry by voluntary agreement among the members of the syndicate had been gaining ground. The matter had been discussed during the year 1913, but not until March of the following year was it brought formally before the organization.[2] After a two-day session in May, 139 of the 169 members of the syndicate signed an agreement not to erect, cause to be erected, encourage, or lend any aid to the erection of new works until after December 31, 1919.[3] Several other works soon fell in line so that within a month, three quarters of the total official allotment was represented by the signers of the contract. The plan was then formally approved by the Prussian Minister of Commerce.[4]

Whether or not the amending bill will become a law is uncertain. The political crisis which has supervened has undoubtedly rendered the potash industry incapable of bearing the burden of the proposed tax, and has rendered immediate action less imperative. The voluntary action on the part of the members of the syndicate promises to prevent the rapid aggravation of the potash situation.[5]

VIII. Conclusion

In its influence on prices, the potash syndicate has differed somewhat from other Kartells. Except for very short periods, export prices have been higher than domestic. Having a monopoly of the products, there has been no necessity for a resort to the "dumping" which has been a practice of the steel and coal Kartells. This has always proved an effective pro-syndicate

[1] K. R., 1914, pp. 195 *et seq.*

[2] *Ibid.*, 1914, pp. 300 *et seq.*; Berliner Jahrbücher, 1913, p. 157.

[3] K. R., 1914, p. 489.

[4] *Ibid.*, 1914, p. 624.

[5] At the opening of the European War, the potash syndicate voted an appropriation of 100,000 marks for national purposes, and placed its organization and press bureau at the disposal of the general staff. K. R., 1914, p. 730.

argument. Prices have certainly been steadied. Statistics of prices show no decline in the price of muriate of potash since the formation of the first agreement in 1879, and none on carnallite since 1888, the date of the formation of the first syndicate.

The potash syndicate has at all times attempted to secure the maximum gain, but has realized that the demand for agricultural purposes is capable of great expansion, and that the highest prices may not be the most profitable. In general, potash prices, though not to be classed as extortionate, are said to have been higher than the demand for the product, the cost of production, or the interests of the industry itself justify. The fact that mines running at much lower than normal capacity could, in 1906, pay dividends averaging 13.5 per cent; that the cost of production was a considerably smaller part of the selling price than in other mining industries; the fact that Schmidtmann and others could contract to deliver large quantities of potash at 30 per cent below prevailing prices, with the expectation of still securing profit therefrom, — all these indicate a range of prices above the competitive level.

The syndicate has had no effect in decreasing the expenses of production; its influence has actually been exerted in the opposite direction. The economies which have been effected by syndicate organization have been in distribution, — elimination of the wastes of competitive selling and increase in the effectiveness of advertising. But, though these savings have been considerable, the syndicate and the legislation enacted in the attempt to check tendencies induced by syndicate policies have contributed to bring into existence such an oversupply of facilities for production that no net gain in efficiency has resulted. Since the demand for potash is only sufficient to give existing establishments employment much below normal capacity, there is good reason to believe that expenses of production are higher than they would be under competitive conditions, and that costs as well as prices would be lower.

Domestic consumers, as noted above, have fared somewhat better than the foreign. The influence of the government mines has always been exerted in the direction of lower prices for domestic consumers. Most favored have been the large agricultural

Year	Price of Carnallite in Marks per Doppelzentner	80 per Cent Muriate of Potash Marks per Doppelzentner	Year	Price of Carnallite in Marks per Doppelzentner	80 per Cent Muriate of Potash Marks per Doppelzentner
1861	1.60	36.00	1881	1.00	12.70–16.00
1862	1.60	30.00	1882	1.00	14.50
1863	0.80–1.60	27.00	1883	1.00	13.50
1864	0.80	24.00–19.50	1884	1.12	13.26
1865	0.80	19.50–12.50	1885	1.12	13.36
1866	0.80	12.50–13.00	1886	1.12	13.32
1867	0.80	12.50–13.00	1887	1.12	13.34
1868	0.80	12.70–13.20	1888	0.80	13.38
1869	0.80	13.00–14.50	1889	0.80	13.43
1870	0.80	13.80–18.50	1890	0.80	13.45
1871	1.10	18.16–18.50	1891	0.80	13.45
1872	0.80–1.20	18.70–16.20	1892	0.90	13.88
1873	0.80	16.00–12.00	1893	0.90	13.88
1874	0.80	13.00–12.50	1894	0.90	13.88
1875	0.80	12.50	1895	0.90	13.88
1876	0.80	12.00	1896	0.90	14.25
1877	0.80	11.00	1897	0.90	14.25
1878	0.80	9.20	1889–1908	0.90	14.70
1879	0.80	11.00			
1880	1.00	11.15			

The figures given in Stange (p. 95), Engelke (p. 38), and Schulze (p. 59) vary slightly from those given above.

associations, — in part, it is alleged, because of their political influence. The favoritism shown to these societies has led to many complaints from potash dealers. The syndicate finally made some concessions to the dealers in 1905, but did not place them in every particular on a footing with the agrarian associations. After 1909, when the restrictions on combination among dealers were removed, a large number of dealers' organizations sprang up to take advantage of the rebates given for purchase in large quantities. But the agricultural associations are still favored. The attitude of dealers has generally been unfriendly to the syndicate.

One must not neglect to give the potash combination credit for what it has accomplished in connection with its propaganda work. By the distribution of publications, exhibits at important agricultural shows, fertilizer experiment stations, and other

methods, it has conducted a general educational campaign on the use of fertilizer, potash especially. The efforts of the syndicate to keep up the standard of the products and to insure prompt deliveries are also commendable.

The membership of the Prussian government has given the potash syndicate a character distinct from other Kartells. Far from being a passive member, the government has always exerted a large influence upon syndicate policy. More than once it has directed its energy toward keeping the organization intact in the numerous crises through which it has passed. In the negotiations of 1879, 1888, 1898, and 1901, the fisc took an active pro-syndicate part; when renewal came up in 1903, the Prussian fisc took the initiative; in 1908, the government early directed its influence toward renewal. It cannot be seriously doubted that, had not the Prussian government played the part it did, the syndicate would early have gone to pieces.

The opinion so often expressed during the progress of syndicate negotiations that in the continuance of the syndicate lay the only means to avoid the ruin of a number of enterprises and losses to thousands of investors, was undoubtedly correct.[1] But one may doubt whether or not it was wise to enter into combination to preserve the profitableness of all the undertakings, when the policy of procrastination, as one might term it, caused and will continue to cause much greater losses. Free competition during the eighties would have been attended with losses smaller than in the decade 1900 to 1910, or none at all. The dependence of the value of potash enterprises upon the existence of the syndicate is clearly shown in the course of the market for potash securities during the past decade. It is reasonable to suppose that under the rule of competition the enormous over-investment of capital in potash enterprises would largely have been avoided. When all is said for and against the syndicate, one may doubt whether the potash industry is, as a whole, in 1913, in a more flourishing financial condition as a result of the existence of combination.

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[1] It is said that bankers would extend credit only to those mines whose intention to enter the syndicate was known. K. R., vol. v., p. 307.

XXIV

THE GERMAN STEEL SYNDICATE[1]

A more elaborate account of the Stahlwerksverband, brought down to date, moreover, is now in process, under the hands of Professor H. R. Tosdal of the Massachusetts Institute of Technology, author of the preceding chapter on the potash cartell. It will form part of a comprehensive treatise on the German industrial syndicates, to be separately published in due time. To Dr. Tosdal, I am indebted for the following comment on this chapter which serves to bring it up to date.

The Stahlwerksverband was renewed in 1907 for a five-year period. The chief difficulties settled temporarily at that time were the change in organization, by eliminating the Beirat, the adjustment of the relations between the individual steel works and affiliated wholesale iron dealers, the rearrangement of freight bases, and the allocation of quotas. The last became increasingly difficult because the first results of a new tendency, that toward overexpansion of productive facilities [illustrated as well in the potash syndicate, just described] began to find expression. The force and effect of this tendency to increase productive capacity beyond demand was such that when renewal in 1912 came up for discussion, it was found impossible to secure the assent of producers to limitation of production in more than one category of products, — the so-called A products. All provisions relative to B products were dropped. The steel syndicate was thereby made less comprehensive and powerful than it was when it commenced operations.

Walker, I believe, regards the Stahlwerksverband as a "good" combination. If one is to form an opinion from the character of its price policy, the judgment of the student in 1914 would be the same. But since Walker wrote, there has taken place the new development mentioned above. In so far as the over-rapid expansion of steel enterprises has been due to the steel syndicate, — and that syndicate influence has been great is undeniable, — the statement that it is a "good" combination must necessarily be modified. The extent to which over-investment and consequent waste has been induced seems to me to have been so great as to neutralize the negative "goodness" of its true policy.

Walker seems to expect the further expansion of the syndicate. As events showed, syndicate friends were gratified to be able to secure renewal in its old form against the opposition of 1907. In 1912, they did not succeed in doing this. The underlying cause for this failure was the fundamental opposition of interests of the two

[1] From *Quarterly Journal of Economics*, XX, 1906, pp. 353–398. The copious scholarly footnotes are for the most part omitted.

classes of concerns which must be induced to enter a combination in order to complete a monopoly. These were the integrated and non-integrated works to which Walker refers.

The student will find comparisons most enlightening between the conditions which in Germany brought about this combination, and those heretofore described in our Chapter V, which almost contemporaneously superinduced the promotion of the United States Steel Corporation. Taussig, Some Aspects of the Tariff Question, 1915, part III, on iron and steel should also be read in this connection. — ED.

COAL and iron are the foundations upon which national industrial greatness is based. Germany is preëminent in both, and in both of them there are powerful combinations. In the coal industry Germany takes the third rank among the nations of the world, but in iron and steel she is second only to the United States. In 1904 the pig iron production of the four leading countries of the world was approximately as follows: the United States 16,781,000, Germany (including Luxemburg) 10,119,000, Great Britain 8,500,000, and France 3,000,000 tons. In steel production Germany has an even greater lead over Great Britain. The present position of Germany is the result of recent developments, which, though rapid, have been very steady.

The two primary natural conditions for the iron industry are ore supply and fuel. In both of these respects Germany is richly endowed. In regard to iron ore production Germany is only surpassed by the United States: in 1904 the total output of iron ore was 22,047,393 tons. The coal output in 1905 (excluding lignite) was 121,190,249 tons. For iron ore production by far the most important district is the "Minette," which lies in Lorraine and Luxemburg, and extends over their borders into France and Belgium. The next most important region is on the right bank of the Rhine in the valleys of the Sieg, the Lahn, and the Dill. The production of ore in the other regions is comparatively small, the two most noteworthy regions being one in the province of Hannover and the Duchy of Brunswick and another in Upper Silesia. There are three great coal regions in Germany. The greatest is that of the Dortmund or Ruhr district, which produces more than half of the total. The

next in importance is Upper Silesia, while the Saar is third. The coal deposits of Lorraine, which are nearest to the great ore deposits of the Minette, are not yet developed. The nearest district of fuel supply is the Saar, but the coal of that region is not well adapted to the reduction of ores. The Minette, therefore, must be reduced by the Ruhr coal, and an exchange is made between the two regions, the pig iron industry being about equally divided between them. The Ruhr also uses a good deal of ore from the Sieg, Lahn, and Dill districts, as well as a large amount of foreign ore. In Upper Silesia the iron ore and coal are found in close proximity, but the supplies of the former are too scanty for the industry of that region, and a large proportion has to be imported, especially from Austria and Hungary. The Ruhr coal district is not only first in the magnitude of its coal output, but also in the quality of the coal, which is especially adapted to the production of coke. In this respect neither Silesia nor the Saar can compare with it. Although the enormous iron ore production of the Minette is of a low grade, its cheapness makes up for the deficiency in iron. The Minette ore is a brown hematite with from 35 to 40 per cent of iron and from 0.04 to 1.96 per cent of phosphorus. The ore deposits are of great depth, and sometimes as much as fifty metres thick. On account of its high percentage of phosphorus this ore was not much valued until the discovery of the Thomas process (basic converter). The ore of Siegerland, red hematite, contains considerable manganese, and is of a high quality.

Although Germany is a large producer of iron ore, she is also a large importer and exporter. In 1904 Germany imported 6,061,127 tons of iron ore and exported 3,440,846 tons. Large quantities are imported for mixing with domestic ores. In the Rhenish-Westphalian district iron ore is used from over one hundred different places, including almost all known sorts, and coming from almost all parts of the world. The usual mixture in this region is Minette, 35-40 per cent; Swedish, 35-40 per cent; red hematite, 10 per cent; and other, 10 per cent. In Silesia a typical mixture is said to be 27 per cent of the local ore with 21 per cent of cinder, 23 per cent of Swedish, and 25 per

cent of Hungarian ore. Another reason for the large iron ore imports is that there are many iron furnaces far from the domestic regions of supply, so that the foreign ore can often be delivered more cheaply.

The distribution of the pig iron production of Germany and Luxemburg is shown in the following table: —

PRODUCTION OF PIG IRON IN GERMANY (INCLUDING LUXEMBURG) IN 1905[1]

Kind	Rhineland-Westphalia, except the Saar and Siegerland	Siegerland, Lahn District, and Hessen Nassau	Silesia	Pomerania	Hannover and Brunswick	Bavaria, Würtemberg, and Thuringia	Saar	Lorraine and Luxemburg	Total
Foundry	891	177	94	155	54	28	83	423	1,906
Acid Bessemer	263	38	48	—	77	—	—	—	425
Steel iron and other Spiegeleisen	330	283	98	1	—	2	—	—	714
Thomas or basic Bessemer	2,868	0[2]	259	—	240	133	731	2,884	7,115
Forge or mill iron	25	213	362	—	—	14	—	213	827
Total	4,377	711	861	156	371	177	814	3,521	10,988

Looking first at the production of the different districts, it will be observed that Rhineland-Westphalia (or the Ruhr) has the largest production in 1905, and that Lorraine-Luxemburg (which includes a large part of the Minette district) is second. Together they produce over 70 per cent of the total. Silesia and the Saar produce only about 8 per cent and 7 per cent respectively. If the table be examined with regard to the kind of iron produced, it will be observed that most of the iron is of Thomas or basic Bessemer steel, — in 1905 over 60 per cent, while foundry iron came second with about 17 per cent, and mill iron or puddled iron third with about 8 per cent. Acid Bessemer steel is almost negligible to-day in Germany. The bulk of the Thomas steel is produced in the German Minette or in the Ruhr, but a not inconsiderable amount is also produced

[1] In thousands of tons: thus 891 = 891,000 tons. [2] 3 tons only.

in the Saar. Most of the foundry iron is produced in the Ruhr and the Minette, particularly in the former. Silesia, which occupies a very subordinate position in other respects, is the chief producer of mill iron. The two leading facts are, however, the great preponderance of the Minette and the Ruhr in the German iron industry and the predominance of Thomas or basic Bessemer steel.

The German steel industry is quite as important in the production of finished products as in the raw material. The distribution of the manufacturing industry does not correspond very closely with the distribution of the blast furnaces. Bavaria, for example, has a large machine industry, but only a trifling output of pig iron. The Minette, though it rivals the Ruhr in the output of pig iron, cannot compare with it in the output of finished products. It is only recently that the Minette has begun to develop the manufacture of rolled products on a large scale. Only about one third of the pig iron produced in the Lahn and Dill valleys is worked up there. In Silesia, however, there is an extensive output of rolled products.

Between the various producing regions there is naturally a lively competition for the German market. Especially for pig iron there tend to be developed certain natural regions of supply determined, in part, by the costs of transportation. This is distinctly the case as between Silesia and the western industrial regions. Silesia controls the supply in the far eastern provinces, where it meets western competition only in finished products. Customs duties prevent it from developing its sales to any great extent into Austria and Russia. For the two great western producing regions, the Ruhr and the Minette, there does not appear to be any distinct recognized division of markets, although the latter region is naturally more directed to the export trade.

Germany is a great consumer as well as a great producer of iron products, and the consumption has increased rapidly with the great development in production, population, and wealth. In 1903 the total consumption was greater than in England, although it was much below that of the United States. Reckoned, however, according to population, the consumption of England was greater than that of Germany. The total con-

sumption depends not only on the production, but also on the movement of imports and exports. Germany is both an importer and exporter of iron products. The movement for 1904 is shown in the following table:

	Imports	Exports
Pig iron and half products	240,233 tons	701,985 tons
Iron manufactures	101,492 tons	2,022,01 tons

The chief imports were pig iron, scrap iron, steel bars, iron for plowshares, and tin plate. The chief exports were pig iron, half products, beams and girders, rails, steel bars, sheet bars and sheets, rods, coarse iron wares, etc. The principal foreign markets for German half products in 1904 were England and Belgium. More than half of the total was destined to England. The exports of rails from Germany, on the other hand, were widely distributed, though England again was the chief market. England was also the chief purchaser for beams and girders. In regard to the official export statistics a great difficulty always exists on account of the fact that the given country of destination is not the country of final destination or consumption. The exports to Holland and Belgium are, in large part, really destined for England.

Although the German iron industry is extremely formidable in international competition, it undoubtedly finds a good deal of its strength in the existence of an effective protective tariff, which secures the home market and enables it to dump its surplus products in the world markets.[1] The protection established for the iron trade has a vital relation to the existence of the various iron and steel combinations. Before the present protective policy for the iron trade was inaugurated, the production lagged far behind the consumption. In 1878 a special committee of inquiry was appointed to investigate the subject, which almost unanimously agreed that protection for the iron industry was necessary, and this conclusion was followed by a law (1879) which imposed duties higher than those recommended, which remained in effect without substantial change down to the recent recasting of the tariff (to go into effect March 1, 1906).

[1] Cf. F. W. Taussig, Some Aspects of the Tariff Question, 1915, pp. 117–216, especially pp. 191 ff. — Ed.

The duties on an ad valorem basis, both in the old and in the new schedules, amount to about 15 per cent on pig iron, 20 per cent on rails, 16 per cent on sheets, and 9 per cent on rods.

There are a number of large iron and steel concerns in Germany which combine with the manufacture of steel the production of the raw materials, iron, ore, coal, coke. But the individual concern has ceased to be the unit in German industry to a large extent. The modern unit is the cartell. The most important matters of commercial and economic policy are determined to-day by these combinations.

Combinations in the German iron industry are of ancient date, and have assumed forms adapted to the contemporary economic organization. The distinction between the early methods of combination and the modern system lies not only in the more comprehensive character of the latter, but also in the fact that the modern iron industry is established on a stupendous scale, and operates for the world market. It is often stated that the first German cartell was the tin plate combination, which was formed in 1862; but this was not the first cartell even in the iron trade. Rail pools existed over fifty years ago. It was not until the seventies, however, that they acquired much importance. There was an overdevelopment of the iron industry at the beginning of that decade, and during the following depression the producers resorted to combinations to restrict their output and to maintain prices. The early cartells were generally quite limited as respects the commodities and the region included in the agreement. The first important exception to this (apart from rail pools) was the combination of German Rolling Mills, which originated in 1886 in Silesia and expanded to include the whole country. It exercised a very marked influence over the German iron trade down to its dissolution in 1893, in the face of new competition. The head of this combination, Caro, declared at the time that it failed because a cartell of rolled products could not stand alone: it was necessary to cartell the raw materials and the finished products also. At that time, however, the producers of raw materials — coal and pig iron — had not been able to extricate themselves from the position into which their previous overdevelopment had brought them. They were

also facing a constant decline in prices, owing to rapid reductions in the cost of production due to technical improvements. The rolling mills and the manufacturers of finer wares were in a relatively favorable situation. They often got their raw material under cost. The large mixed works, or those which combined the production of raw materials with the manufacture of commercial products, complained of the disadvantage at which they were placed as compared with the straight rolling mills (*reine Walzwerke*). There was no advantage at that time for a rolling mill to acquire coal mines or to establish blast furnaces, and hence the policy of combining the various stages of production, which had been quite conspicuous at an earlier period in the Ruhr district, did not find frequent illustration at this time.

Fundamental changes appear in the general conditions of the industry at the beginning of the nineties. A tolerably successful pig iron cartell had been established in the Ruhr in 1886, but it was not until the Coke Syndicate was accomplished in 1890 that a secure basis was formed. The iron industry was still in a weak position. In 1892 the pig iron producers of the Ruhr and the Minette got together, while a pig iron cartell was formed in Siegerland two years later. The ore production in Siegerland was combined in the same year. In the Minette the ore was almost entirely controlled by the blast furnaces. More important than all of these was the formation of the Coal Syndicate in 1893. This powerful combination dominated the whole industry during the ensuing decade. Thus the foundations were laid for a new régime in the iron trade, in which those who controlled the raw materials were to have a great advantage. The days of cut-throat competition between mining companies, in which the iron manufacturer could speculate on the demand for finished products with the assurance that the raw material would be abundant and cheap, were over. The new fuel cartells were founded on the principle of monopoly control, and the pig iron cartells partook, to some extent, of that character also. The combinations among the manufacturers of iron products did not keep pace with these developments among the producers of raw materials. The cartell of German Rolling

Mills was dissolved in 1893, and no general combination appeared to take its place. The rail pool seems to have maintained a continuous existence, but the beam pool was dissolved about 1892, though reorganized shortly after.

In 1894–1895 a marked improvement appeared in the commercial situation in general, and in the iron trade in particular, which lasted until 1900. Although some of the earlier cartells may have been "*Kinder der Noth,*" the period of prosperity furnished apparently a healthful environment for growth.

The most important event of this period was the establishment of a half products cartell. This innovation was a consequence of new technical conditions, and particularly the development of great steel mills for the production of Thomas or basic steel. The characteristic products of these steel mills are rails, beams, and half products (ingots, billets, sheet bars, etc.). The half products are the raw material of the rolling mills. The large steelworks found that the straight rolling mills were not keeping pace with their development, and that it was safer, as well as more profitable, to work up their own crude steel to a large extent. They were generally mixed works, controlling their own supplies of fuel, ore, and pig iron. These works formed the Half Products Syndicate (*Halbzeugverband*), and this cartell, combined with the rail and beam pools, was the immediate forerunner of the present Steel Syndicate. At first, however, they had a price agreement simply, and it was somewhat later (1899) that the sale of half products was syndicated. This cartell soon included all the great steelworks of western Germany. The works supplied the straight rolling mills with their raw material, and at the same time competed with them in the manufacture and sale of rolled products. This put the rolling mills in a dangerous position, because, technically, they were no match for the great steelworks. In 1897 a comprehensive but complicated cartell was established between the pig iron producers of the Ruhr, the Minette, and Siegerland. In the period between 1895 and 1904 the principal cartells established for rolled products were as follows: heavy sheets and rods in 1897, wire nails in 1898, and light sheets in 1902. The rolling mills failed, however, to cartell steel bars. In Silesia rolled products were effec-

tively cartelled ever since 1887, in one form or another. These cartells do not comprise, by any means, all of those found in the steel industry during this period, but were the most important connected with the development of organization in the steel trade.

The development of cartells in various steel products called forth protective organizations among the consumers. An important organization of this sort was the Rhenish-Westphalian Purchase Association for pig iron, which was established in 1901. More important than this was the Association for the Protection of the Interests of the Consumers of Half Products which was formed in 1902. This included forty-two concerns, mostly straight rolling mills, with a demand (in 1903) for 560,000 tons. There were numerous other purchasing combinations, especially during the recent crisis.

The reasons for the formation of the Steel Syndicate, according to an official statement made to the government, were substantially as follows: The discovery of the Thomas or basic process had made practicable the utilization of the immense deposits of phosphoric ore in the Minette district, and had given rise to a number of large steelworks adapted to that purpose. This, in turn, had induced the existing steelworks to modernize and enlarge their plants, which caused an overproduction of steel, and imposed upon the steelworks the necessity of combining to restrict their output. The earlier efforts in the way of price agreements proved ineffectual, and made necessary the establishment of stronger combinations. Strong cartells thus established in various steel products proved defective also, because they lacked control over the export trade, as well as a comprehensive oversight of the market. The Steel Syndicate was formed, therefore, with the intention of bringing about a harmonious action in all lines of steel production. The first step was to secure an effective combination of the heavy rolled products (half products, rails, and structural steel), and these products could be more easily brought into a combination because they were made to a great extent by a limited number of large mixed works, which had a certain economic likeness. The next step was to bring about a cartell for the light rolled prod-

ucts. This, however, had not gone beyond a determination of quotas, and awaited an agreement with the outside straight rolling mills and the Siemens-Martin (open hearth) steel mills before it could be firmly established.

The project for the Steel Syndicate was first broached in a practical sense in the autumn of 1902. The chief spirit in the movement was Adolf Kirdorf, the head of the Half Products Syndicate. After preliminary preparations a meeting was held in February, 1903, which chose a commission to work up a plan. This plan came up for acceptance in the autumn of the same year. There were the usual protracted negotiations, but finally all of those works whose adhesion was regarded as vital were secured by various compromises and concessions, except Krupp, Phoenix, and Westfaelische Stahlwerke. The agreement was ratified nevertheless on March 1, 1904, and almost immediately after Krupp joined in consideration of an enlarged quota. It was deemed essential, however, that Phoenix should enter the combination, and the newly formed Syndicate applied all its commercial and financial influence, especially with the Coal Syndicate and the banks, to achieve its purpose, treating it as a "scab" concern. The management of Phoenix refused to join because they regarded the quota allotted to them as insufficient. The Syndicate soon succeeded, chiefly through the influence of the great banks, in getting the shareholders of Phoenix to reverse the policy of the management. The vigorous and drastic measures which the syndicate took to accomplish its purpose excited a good deal of unfavorable criticism, but Phoenix has accepted the situation with a tolerably good grace. As a matter of fact, its profits have shown a large increase.

The Stahlwerksverband went into effect on March 1, 1904. It was concluded for a term ending on June 30, 1907; and, in case there is no written objection to its continuance by any member before December 31, 1906, it is to stand until June 30, 1912. The character of this agreement, in respect to matters of general interest, is substantially as follows:

The steelworks owners in the combination have an agreement whereby they obligate themselves to sell certain products to their central company, which is called the Stahlwerksverband

They agree further to meet in a general assembly to perform certain duties imposed by the agreement on that body, and also to submit to the directions of certain organs provided for in the agreement. The Stahlwerksverband, or central company, has, on its part, an agreement with the steelworks owners to purchase all of their products, of the kinds specified, and to sell them again under the terms fixed for the agreement. The Assembly of the Steelworks Owners elects an Advisory Council (*Beirat*), a body called the Commission, and several subordinate commissions. The Stahlwerksverband has the usual statutory organs of a company; namely, Supervisory Council, Managing Directors (*Vorstand*), and General Assembly. In the Assembly of Steelworks Owners each member has one vote for every 10,000 tons quota of production. Some of the chief powers of this body are: (1) election of Beirat and Commission, (2) admission of new members, (3) determination of eventual restriction of quotas, (4) assent to sales or leases of plants by owners, (5) determination of penalties, (6) dissolution of agreement in case of reappearance of competition, and (7) provision for the inclusion of light rolled products (B-Products) in syndicate sales. The Beirat is composed of members elected by the Steelworks Owners, each owner or group of owners having the right to elect one member for every 500,000 tons of quotas. The members of the Beirat must be chosen from the General Assembly. The chief powers of the Beirat are (1) holding members of the combination to their agreement, (2) provision of rules regarding selling prices and terms of sale, (3) determination of increase of quotas for B-Products (see below), (4) determination of prices to be paid the Steelworks Owners, (5) disposition of reserves, (6) imposition of penalties, and (7) authorization to Vorstand to conclude agreements with competitors, etc. The third organ of the cartell is the Commission, which is composed of eight members, and which has the following powers: (1) classification of commodities, and (2) determination of "scale prices," comparative weights and compensation for unusual specifications. Among the subordinate commissions the freight commission may be specially mentioned.

The selling company is called the "Stahlwerksverband

Aktiengesellschaft." It is located in Düsseldorf. The purpose of the company, as described in the by-laws, includes not only the purchase and sale of iron and steel products of all kinds, but also the acquisition and operation of all kinds of enterprises which are connected with the storage and transportation of iron and steel products. This company has a share capital of 400,000 marks in registered shares, which are not transferable with the consent of the General Assembly. This capital is nominal in amount, because the company, although it does an enormous business, is, in effect, only an agent of the Steelworks Owners, and sells for cash. The Managing Directors, or the *Vorstand*, conduct the business of the company, which has a very large and highly organized bureau. There is one department for accounting, statistics, taxation, freights, legal work, and for dealing with the public authorities, and a department for the sale of each of the three kinds of heavy rolled products.

The commodities covered by the agreement are specifically described. They include (1) the production of crude steel and forge iron; (2) the purchases of the same, and also of rolled half-products and products enumerated under the two following specifications; (3) the production of half products, railway material, and structural steel; (4) the production of bars, rods, heavy and light sheets, tubes, railway axles, wheels and tires, forge pieces, cast steel pieces, etc., so far as not made from material under 3 and 4, but directly from crude steel; and (5) the purchase from Steelworks Owners of commodities enumerated under 3, if they are for the plants of the Steelworks Owners, and if the products thereof are sold by the cartell. The products enumerated under 1 and 3 are called A-Products, and those under 4 are called B-Products. The Stahlwerksverband buys from the Steelworks Owners all the products which are offered for sale under the group A-Products, and sells the same for the general account. For B-Products, on the other hand, the amount of production is fixed, but the sale is left to the Steelworks Owners individually, or to such other cartells as they may belong to.

The quotas of the Steelworks Owners for the A-Products

sold by the Stahlwerksverband are based on the amount of crude steel originally allotted to each by the agreement. This is called the principal quota, and is divided into three "group quotas"; namely, (1) crude steel and half products for direct sale, (2) railway material, and (3) structural steel. The group quotas are given in crude steel equivalents. It is the duty of the selling company to distribute the orders so that each concern shall have its share according to its quotas. There are various particular provisions in this connection. If the total of the quotas is increased, they must all be increased in proportion; but, if any concern is unable to maintain the increased output allotted to it, the works which produce the excess are required to pay those which produce less a contribution of 5 marks per ton. Certain exchanges in quotas between different plants are allowed, with the consent of the Vorstand, and it is also provided that the Vorstand can make arrangements whereby certain works shall receive the bulk of orders for unusual specifications. Both these provisions aim at a greater economy of production by a division of labor. Each Steelworks Owner must fulfill orders allotted him; but, in case they involve changes in his equipment, compensation must be made. Where a concern uses its own products, the Stahlwerksverband does not intervene as a buyer or seller.

The selling prices are fixed by the Vorstand under the guidance of rules laid down by the Beirat. The Steelworks Owners receive a minimum price ("table price") originally, and afterward what excess remains from the actual proceeds after deduction of the various expenses of administration, reserve, rebates, etc., incurred by the selling company. It is evident that the only way open for any particular concern to increase its profits is to reduce its costs of production. The "table prices" are for Thomas or basic Bessemer steel. Extra prices are allowed for commodities of superior grade, based on the extra proceeds of sale. A particular concern may receive higher prices than others if it is clear that its product commands a higher price in the market on account of quality. Important features of the price regulation are the freight-basing points. In the domestic trade the rules are as follows: for half products there are five

bases, and the purchaser is quoted a price from the base nearest to his works; for railway material the base is the producing concern; for structural steel the base is Diedenhofen. In the foreign trade the basing point is the plant most favorably located for the purchaser. These rules represent partly compromises between different interests in the combination and partly attempts to economize freight charges. For the foreign trade, for example, each concern has the advantage or disadvantage resulting from its geographical situation with regard to the destination. In domestic railway material, on the other hand, geographical situation has no effect. Export bounties which are received from other cartells (*e.g.* Coal Syndicate or Pig Iron Syndicate) are distributed in such a manner that the Steelworks Owners who make the commodities for which export bounties are received get their share thereof, whether their products are exported or not.

For the B-Products the principal quota is the weight of crude steel required to make them. This is fixed for each concern in the original agreement. A concern can reduce its sale of B-Products at will. On the other hand, it cannot increase its sales without leave from the Beirat. If a concern sells more than its allotted quota, it must pay 20 marks per ton for such excess sales.

The agreement provides for a "reserve," which is intended principally for the promotion of the export trade or for fighting competitors. It is acquired by deductions made from the proceeds of sale on the basis of the "table prices." This assessment is fixed by the Assembly of Steelworks Owners, with the limitation that it cannot exceed 3 per cent of the sums paid under the "table price" payments. The Steelworks Owners are prohibited from selling or leasing their plants without the consent of the Assembly of Steelworks Owners, but this assent must be given if proper guarantees are provided for the fulfilment of cartell obligations. On the other hand, the Steelworks Owners are forbidden to buy or operate any outside plant that makes A- or B-Products or to erect new plants for the production of those commodities. The Vorstand has the right to supervise all concerns, and to inspect plants, books, and papers, in

order to insure due performance of obligations. Detailed provisions are made regarding fines and penalties. An arbitration court is established also, which (to the exclusion of the courts of law) has jurisdiction over disputes concerning the obligations of the parties to the agreement. In case new competition appears during the term of the cartell with a production amounting to 5 per cent of the cartell in A- or B-Products, according to the opinion of the Beirat, the agreement may be canceled.

The original quotas of the members of the Stahlwerksverband for different products are shown in the table on opposite page.

In addition to the quotas given above, certain concerns have the privilege of purchasing a fixed amount of steel. The only important allowance is that of Phoenix, which amounts to 100,000 tons. Besides this certain other works are to receive in the future certain additions to their quotas. Here, again, there is only one case in which a considerable increase is provided for; namely, Krupp, which by April, 1907, will be allowed 706,000 tons for its total quota. Taking the total quotas, the geographical distribution is as follows: for the Rhenish-Westphalian works, 54 per cent; for the works in the Saar, Lorraine, and Luxemburg, 32 per cent; for Upper Silesia, 7 per cent; and the remainder (7 per cent) in various parts of Germany.

The proportion of the production of the Stahlwerksverband to the total production of Germany is estimated at about 90 per cent. All the important steelworks which were deemed to come within the scheme of organization except one — the Westfälische Stahlwerke — are included in the agreement. Several works have been added since then. There does not seem to be any immediate likelihood of new competition appearing. To start a new first-class steelworks with an independent supply of coal and coke would cost, it is said, fifty million marks. Voelcker says, "The German Stahlwerksverband represents for the cartells in the iron industry, not the keystone of the arch, but rather the foundation of a new grouping." The chief purposes of the cartell are officially stated to be (1) the maintenance of the domestic market, (2) the full occupation of the works, (3) the simplification of working programs of the works, and (4) the elimination of competition among German works in

QUOTAS IN THE STAHLWERKSVERBAND (IN THOUSANDS OF TONS)

(*Jahrbuch für den Oberbergamtsbezirk Dortmund*, 1901–04.)

Company	A-Products	A-Products: Half Products	A-Products: Railroad Material	A-Products: Structural Steel	B-Products	B-Products: Bars, etc.	B-Products: Rods	B-Products: Plates and Sheets	B-Products: Tubes	B-Products: R.R. Axles, etc.	Total A- and B-Products
1. Deutscher Kaiser, Thyssen & Co.	285	50	133	102	419	253	29	93	43	3 [4]	704
2. Königs u. Laurahütte 3. Oberschlesische Friedenshutte	140	in B	85	55	335	244	—	80	31	10	475
4. De Wendel & Co.	248	65	53	131	212	129	24	58	—	[6]	460
5. Fried. Krupp	234	90	144	—	222	50	7	40	3	122	456
6. Hörder Verein	250	122	63	65	175	55	—	103	—	17	425
7. Gutehoffnungshütte	202	49	110	43	206	74	34	76	—	22	408
8. Rombacher Hüttenwerke	341	217	48	76	38	38	—	—	—	[6]	379
9. Rheinische Stahlwerke	251	111	100	40	134	66	—	54	—	13	378
10. Aachener Hütten Akt. V.	214	77	49	88	119	101	17	—	—	1	333
11. Dortmunder Union	229	59	114	56	104	90	—	—	—	14	323
12. Eisen u. Stahlwerk Hoesch	152	38	63	51	169	102	20	41	—	6	321
13. Bochumer Verein 14. Ges. f. Stahlindustrie	143 73	55 18	87 52	1 [3] 2	91	15	—	—	—	76	306
15. Burbacher Hütte	194	10	55	129	99	84	15	—	—	—	293
16. Rochlingsche Werke, Volklingen	192	37	50	105	101	75	26	—	—	—	293
17. Gebr. Stumm	172	25	62	85	121	95	26	—	—	[7]	293
18. Peiner Walzwerk	165	15	5	145	88	76	—	—	—	—	253
19. Lothringer Hüttenverein, Aumetz-Friede	210	128	27	55	30	30	—	—	—	—	240
20. A. G. Differdingen	149	71	23	55	70	30	40	—	—	—	219
21. Eisenhütten Verein, Dudelingen	191	111	40	40	20	20	—	—	—	—	211
22. Dillinger Hüttenwerke	91	61	30	—	97	—	—	88	—	9	188
23. Maximilianshütte	109	17	54	38	55	33	—	12	—	—	164
24. Hasper Eisen u. Stahlwerk	25	7	—	17	76	41	35	—	—	—	101
25. Eisenwerk Kraemer	40	—	27	14	60	60	23	—	—	[6]	94
26. Georgs-Marien-Verein	62	[1]	61	—	14	2	—	—	—	12	75
27. Van der Zypen	23	6	1 [2]	16	47	28	—	—	—	19	70
28. Phönix	166	50	116	—	350	120	140	70	—	21	416
29. Kattowitzer A. G.	25	—	5	20	50 [9]	50 [9]	—	—	—	—	75
30. Sächsische Gussstahlfabrik	24	—	24	—	24	19	—	—	—	5	48
31. Huldschinsky'sche Hüttenwerke	15	—	5	10	—	—	—	—	—	—	15
Total	4614	1490	1685	1438	3522	1976	435	715	47	349	8012

The figures in this table are given in thousands of metric tons to the nearest thousand, but for small quotas this does not indicate them with sufficient accuracy. For the small quotas thus affected the precise figures for the corresponding numbered references are
[1] 300. [2] 1200. [3] 1100. [4] 2500. [5] 400. [6] 200. [7] 161. [8] 400. [9] That is, up to 50.
The addition of the column for tubes does not check, which is presumably due to a typographical error in the authority quoted.

foreign markets. Adolf Kirdorf was elected as the first head of the Syndicate.

It is difficult to estimate the capital value of the concerns in the Steel Syndicate. They include, of course, besides steel mills, coal mines, coke works, blast furnaces, etc. If the share capital at the market quotation is taken, and to this is added the outstanding funded debt, a fairly representative figure is obtained. On this basis, using figures chiefly for 1904, the following computation has been made from the date in the *Dortmunder Jahrbuch* and *Saling's Boersenpapiere*. For twenty concerns in the Syndicate, embracing 63 per cent of the total quotas for A- and B-Products, the total capital value is computed to be about 958.27 million marks. If the same proportion be applied to the aggregate quotas of the syndicated concerns, the total capital value would amount to 1521 million marks, or about $362,000,000.

The Steel Syndicate aimed at a national organization of the industry, and several concerns in Upper Silesia were included in the combination. The steel producers of that region, however, went further, and established a local organization, which in some respects was more complete than the Steel Syndicate. The distance of Upper Silesia from accessible markets makes it necessary for the steel works to manufacture the finer products which pay better for distant shipment. The German Rolling Mill Cartell, which was dissolved in the early nineties, left behind it in Silesia a local cartell which included all but one concern, and this organization lasted down to the end of 1904. It was, however, inadequate, and hence some of the Silesian works joined the Steel Syndicate. This led to the organization of a local steel combination on December 16, 1904, which went into effect at the beginning of 1905. This was called the Oberschlesische Stahlwerksverband G. m. b. H. It includes the eight steel works of Upper Silesia, one in Berlin, and one in Danzig. The term of the agreement is fixed from January 1, 1905, to June 30, 1907, although an earlier dissolution was possible under certain contingencies. The agreement in its general form is modeled on that of the greater Steel Syndicate, but it differs in one very important particular. As there is little of crude steel or heavy rolled products made for sale, these are

not syndicated, but the light rolled products are cartelled instead. Some of these light rolled products are sold by the syndicate, but the others are simply regulated as to output. There were some difficulties in the beginning which threatened to break it up, but these were settled, and soon after the five remaining steel works in Upper Silesia became members of the larger or "German" Steel Syndicate.

One of the characteristic developments of industrial combinations has been the suppression of the middlemen. The Steel Syndicate furnishes some striking illustrations of this fact. Before the formation of the syndicate the dealers in structural steel had been organized in five groups by the Bean Syndicate and these groups were recognized by the Steel Syndicate after it was established. The members of these groups of dealers agree to sell according to certain minimum prices and conditions, and each group has a distinct territory. Similar organizations have been formed in Switzerland, Denmark, Sweden, and Norway. The Steel Syndicate declares that its special purpose in promoting and recognizing them has been to obtain a better view of the market, and to exercise a greater control over it. The dealers have submitted to the inevitable with what grace they could, but they complain that the profit (a commission practically) is too small. For the other products, which the syndicate sells directly, — namely, half products and railway material, — the conditions of trade are different; *i.e.* they are both sold direct to the consumers in the domestic market, and also to some extent abroad. In the most important foreign market of the syndicate, — namely, London, — the former agents of the various companies have been organized into a limited liability company over which the syndicate has taken pains to secure complete control, both of *personnel* and stockholders. Similar agencies have been established to represent the syndicate in Amsterdam and at Brussels. Further, in order to get a better view of the English market, the syndicate has stopped selling f. o. b. Continental ports, and sells instead c. i. f. English ports. The syndicate has even introduced sales with delivery at works to the English consumer.

It would be difficult to appreciate properly the policy of the

Steel Syndicate, especially on account of the brief term of its existence, without some reference to the previous movement of production and prices. Before speaking, however, of any particular feature, it is desirable to note a few of the leading facts regarding the steel market in recent years. The period since 1895 may be approximately described as follows: From 1895 to 1900 there was a great boom, which culminated in a short period of high prices in 1899–1900, and terminated in a crisis in the latter year, which brought on a general and very serious collapse. A period of depression followed, which may be said to cover the years 1901 to 1902. During 1903 improvement was evident, and since then the steel trade has been active, if not, generally speaking, remarkably profitable. The last half of 1905 has brought an extraordinary revival of activity.

The raw material cartells had established themselves at the beginning of the period, and occupied a favorable position throughout. The cartells which existed in finished products were generally more loosely formed, and their policy both in production and prices was less conservative. When the depression came, they were in a weak position, and were more eager to form combinations. The raw material cartells had, however, the advantage, and succeeded in shifting the greater part of the losses occasioned by the hard times on to the manufacturing branches. The former were able, that is, to maintain their prices to a large extent, while the latter had to reduce theirs, and to accept greatly diminished margins. The general policy of all producers was to keep up their production, and to sell abroad at any cost what they could not find a market for at home. The table on opposite page shows the movement of production in some leading lines.

An inspection of this table shows a great increase between 1895 and 1900 for all the products given, except rods and tin plate. The decrease in production in 1901 is equally general, with a slight recovery in 1902. With 1903 production quite generally forged ahead of previous figures, and has continued to increase since. The steadiness with which production has increased in Germany is remarkable. Voelcker states that the normal increase in the demand for steel in Germany is about

PRODUCTION OF PIG IRON AND CERTAIN IRON MANUFACTURES IN THE GERMAN CUSTOMS UNION, 1895–1904[1]

Year	(1) Pig Iron	(2) Cast-Iron Wares, Second Casting[3]	(3) Half Products (from Converter or Siemens-Martin) For Sale	(4) Rails	(5) Finished Products (from Converter or Siemens-Martin)	(6) Wire Rods (from Converter or Siemens-Martin)	(7)[2] Tin Plate
1895	5,465	1,146	1,132	495	2,830	502	31
1896	6,373	1,355	1,358	583	3,462	549	34
1897	6,881	1,440	1,273	799	3,863	513	31
1898	7,313	1,573	1,428	819	4,353	476	35
1899	8,143	1,758[4]	1,508	808	4,820	512	34
1900	8,521	1,785	1,536	922	4,757	457	31
1901	7,880	1,503	1,648	849	4,486	523	36
1902	8,530	1,506	2,230	945	5,101	574	42
1903	10,018	1,704	2,412	1,080	5,802[6]	——	45
1904	10,058	1,987	2,374[5]	——	5,976	——	48

[1] [In thousands of tons: thus 5,465 = 5,465,000 tons.]

[2] Columns (1), (2), (5), *Jahrb. f. d. O. Dortmund* 1901–04, p. 728. Columns (3), (4), *Enquete, S.V.*, Anlage 7. Column (6), *Enquete*, VIII., p. 717. Column (7), *Enquete*, IX. p. 161.

[3] Excluding trifling production in Luxemburg, except in 1904.

[4] Obvious error in original corrected.

[5] *Jahrb. f. d. O. Dortmund*, 1901–04, p. 728.

[6] Excluding 135,699 tons in Luxemburg.

420,000 tons per annum. The pig iron production in Germany during the nine years ending 1904 increased at an average rate of 510,000 tons per annum. The production of pig iron in 1904 showed practically no increase over 1903, while half products declined slightly.

The production policy of the Steel Syndicate during the period of two years since its establishment has not been characterized by any extraordinary features. The syndicate has published the statistics of production only for A-Products. The shipments of these products (reckoned in crude steel weight) were as follows:

March 1, 1904, to February 28, 1905 (12 mos.) . . .	4,533,805 tons, A-Products
March 1, 1905, to December 31, 1905 (10 mos.) . . .	4,517,512 tons, A-Products

The production of the first business year was about 1.4 per cent less than the quotas prevailing for that period. The production for the first *eight* months of the second business year, however, was about 9.9 per cent greater than the prevailing quotas for that period. For the chief subdivisions of A-Products the shipments, reckoned in crude steel weights, were as follows:

Period	Half Products	Railway Material	Structural Steel
March 1, 1904, to February 28, 1905 (12 mos.)	1,599,598 tons	1,394,623 tons	1,529,435 tons
March 1, 1905, to December 31, 1905 (10 mos.)	1,661,649 tons	1,399,960 tons	1,455,903 tons

Comparing the same periods, the shipments during the first ten months in the second year exceeded the shipments during the first ten months of the first year as follows: for all A-Products by 18 per cent, for half products by 23 per cent, for railway material by 20.4 per cent, and for structural steel by 11 per cent. The production policy of the syndicate as indicated by these figures shows a decided tendency towards expansion. It is instructive to compare the policy of the Steel Syndicate with the Half Products Syndicate which preceded it. The following figures for half products are in *finished weights*:

Period	Sales of Half Products, Finished Weights
March 1, 1902, to February 28, 1903	1,460,637
March 1, 1903, to February 28, 1904	1,449,698
March 1, 1904, to February 28, 1905	1,411,903

The sales in 1904–05, under the régime of the Steel Syndicate, were less than those of the Half Products Syndicate. This reduction came out of the export trade, and not out of the domestic supply, as is shown by the following table of domestic sales:

Period	Domestic Sale, Half Products, Finished Weights
1902–03	737,621 tons
1903–04	844,629 tons
1904–05	1,018,277 tons

The data regarding the movement of B-Products are very meager. The syndicate does not generally give out these figures. Kollmann, however, gives a statement of shipments of B-Products during the first year of operation, together with the quotas, as follows:

B-Products	Shipments	Quotas
Bars	1,718,211 tons	1,847,622 tons
Rods	371,713 tons	434,230 tons
Sheets	682,889 tons	714,927 tons
Axles	306,599 tons	351,546 tons
Tubes	48,226 tons	53,400 tons

At the end of March, 1905, the syndicate voted to increase the quotas for bars and sheets by 5 per cent. This increase became permanent on July 1, 1905. The total allotment for A-Products on July 1, 1905, was 4,864,485 tons, as compared with 4,614,225 tons shortly after the formation of the combination. The addition of five more concerns in Upper Silesia increased the total to 4,900,000 tons. In January, 1906, the quotas for bars and sheets were increased again by 5 per cent, while the quotas for rods were increased 10 per cent. The total increase of quotas over the original quotas are as follows: bars and rods, 10 per cent; sheets, 15 per cent.

The movement of prices in the steel trade has been affected in an important degree by the existence of cartells for the various products, but their influence on prices has been very unequal, and none of them ever had complete mastery of the situation. The following table shows the general course of development for the chief raw materials and the chief manufactured products during recent years:

PRICE OF IRON, IRON PRODUCTS, AND RAW MATERIALS[1]

Year	(1) Minette Iron Ore	(2) Blast Furnace Coke	(3) "Fett" Coal Mine-run	(4) Thomas Pig Iron (Westphalia)	(5) Mill Iron (Silesia)	(6) Thomas Ingots Crude		(7) Thomas Billets	(8)[2] Rails
	Aver. per ton	Aver. per ton	Aver. per ton	Aver. per ton	Aver. per ton	Jan. per ton	July per ton	Jan. per ton	Aver. per ton
1895	3.30	11.00	8.00	45.63	—	—	—	—	—
1896	3.30	12.02	8.25	56.58	57.5	72	75	81	—
1897	3.40	13.87	8.85	56.50	61.7	81	84	90	103–5
1898	3.55	14.00	9.08	60.00	61.6	83	83	93	108
1899	3.55	14.37	9.37	70.25	75.7	87	105	97	108–127
1900	3.90	21.29	10.25	91.20 to 71.80	90.7	117	125	127	130–140
1901	4.40	22.00	10.25	90.20	66.5	97	78	107	100–120
1902	2.85	15.00	9.60	57.13	60.8	75	82.50	90	100–105
1903	—	15.00	9.38	57.21	—	77.50	77.50	90	105–130
1904	—	15.00	9.38	57.80	—	77.50	77.50	90	—

Year	(9) Beams		(10) Bars		(11) Rods		(12) Boiler Plate	(13) Light Sheets	(14) Tin Plate
	Jan. per ton	July per ton	Jan. per ton	July per ton	Jan. per ton	July per ton	Aver. per ton	Aver. per ton	Aver. per ton
1895	—	—	95	95	93	93	152.50	121.67 to 128.69	292.3
1896	90	98	105	120	107	112.50	171.66	142.08 to 146.25	301.2
1897	103	105	130	130	122.50	112.50	179.79	127.08 to 133.75	292.9
1898	108	108	117.50	120	123	123	186.25	127.10	289.2
1899	108	120	132.50	172.50	125	150	195.00	184.00	329.4
1900	130	140	185	190	185	185	210.42	197.50	398.0
1901	120	112.50	120	105	150	135	180.00	160.00	340.6
1902	100	105	105	112.50	125	130	158.33	140.17	358.0
1903	105	105	105	110	120	120	150.00	135.88	331.3
1904	105	105	—	—	112.50	—	151.00	125.00	—

[1] In Marks.

[2] Column (1), Bosselmann, pp. 37, 38, 42. Columns (2), (3), (4), (12), (13) *Jahrbuch f. d. O. Dortmund*, 1901–04, pp. 696, 733 (iron prices in 1901 normal). Column (5), Kuh, p. 222. Columns (6), (7), (8), (9), *Enquete, S. V.*, Anlage 7 (rails, domestic prices at Düsseldorf). Column (10) Voelcker, *Bericht*, pp. 130, 131. Column (11), *Enquete*, VIII., pp. 742–747. Column (14) *Enquete*, IX., p. 182.

This table does not present, of course, the details of price movements, and, in general, it does not show the extremes. For example, pig iron was quoted as low as 45 m. in 1901 In Silesia sheets were from 205 to 215 m. at the beginning of 1900, and from 125 to 135 m. at the end of the year. To a very considerable extent, also, rebates were granted on the prices quoted, and even on the material previously sold. Most of the coke was sold for 1900 and 1901 on two-year contracts at 17 m.; and, though the market quotations ran higher, very little was bought on that basis.

An inspection of the price table shows that there was a general advance in prices from 1895 to 1900. The crisis developed in the middle of the latter year. The advances appear quite as early for the manufactured products as for the raw materials, and, on the whole, it may be safely asserted that they were the result of general economic influences, and that there was no causal relation between them. Dr. Voelcker, in his impartial and judicious summary of the situation, declares that from 1895 to 1898 the cartells followed a moderate price policy, but that from 1899 to 1901 the reverse in general was true. The uncartelled lines got high prices in 1899 and 1900, owing to the favorable market, and the cartelled lines were unable to resist the temptation to put up their prices to an immoderate height also. The fall in prices, after the depression set in, was relatively greater for the manufactured products than for raw materials or half products, and it came sooner. This was partly due to the fact that the raw material cartells took advantage of their strong position to make their customers take their supplies on long term contracts; but the latter were also to blame, as they were overanxious to get supplies, not suspecting that a crisis was imminent. The two chief offenders were the Coke Syndicate and the Pig Iron Syndicate. The Steel Syndicate, at the beginning of its operations, established a scale of domestic prices for certain standard products of basic steel. The most important prices were as follows:

Crude ingots . . .	77.50 m. per ton	Structural iron	105.00–108.00 m. per ton
Rolled ingots (blooms)	82.50	Rails	112.00
Billets	90.00	Ties	105.00
Sheet bars	92.50		

These prices prevailed without essential modification until November, 1905. A comparison of these prices with those of the years immediately preceding (1902 and 1903) and the years before the boom acquired much headway (*e.g.* 1896 and 1897) tends to show that the price policy of the Syndicate has been moderate. English reports announce, however, a general 5 shilling advance for half products of the Steel Syndicate in November, 1905, and predict a further rise. These prices look rather high. The price policy of the syndicate, as far as the domestic market is concerned, was enunciated by one of its directors, Dr. Voelcker, as follows: "We do not intend to allow our prices to change continually with the fluctuations of the market. We do not desire, namely, to raise our prices suddenly and rapidly, if the conditions are very favorable; we do not wish, on the other hand, to reduce our prices in bad times, with a declining demand; we desire to keep the middle course."

The syndicate does not fix the prices of light rolled products. The price movement for some of the principal lines is shown in the following table:

PRICES OF LIGHT ROLLED PRODUCTS[1]

Date	Bar Steel (Converter)	Hoops	Boiler Plate (Converter)	Light Sheets (Converter)	Rods (Converter)
1904					
January 1	107–110	12.250–127.50	150	115	112.50–117.50
April 1	112	125–130	155	115	112.50–117.50
July 1	112–115	122.50–127.50	150	115	120
October 1	110–112	122.50–127.50	150	115	112.50–117.50
1905					
January 1	106–108	122.50–127.50	150–155	115	112.50–117.50
April 1	110–115	123	150–155	120–122.50	125
July 1	110	123–125	—	115–120	125
October 1	110–112	125–127.50	130	112–120	125
December 1	112–115	125–127.50	130–135	122.50–125	127.50
1906					
January 1	115–118	130–132.50	130–135	126–130	132.50

A distinct upward movement is observable in the last half of 1905, to which boiler plate forms an exception. This corresponded to an increase in consumption, especially in the domestic

[1] In Marks.

market. Comparing these prices with those of preceding years, the prices of bar steel were unduly low; and the same is true also for light sheets and for rods in 1904. In 1905 the prices of light sheets moved erratically, and were, on the whole, too low, while the prices of rods advanced to a reasonably good basis. The position of steel bars became tolerably good only at the beginning of the year 1906.

The burning question of the steel trade since the crisis has been the position of the straight rolling mills (*reine Walzwerke*) with reference to the mixed steel works (*gemischten Werke*). The latter are the great works which generally have their own raw materials, and combine the manufacture of heavy and light steel products. Though for a time in the seventies and eighties this integration in industry fell into some disfavor, it is accepted to-day in Germany, as elsewhere, as the necessary basis for large and successful operations. Of the 31 original members of the Steel Syndicate, 17 produce coal, 25 iron ore, and 27 pig iron. These large steelworks produce also the bulk of the light rolled products. For example, they produce about three-fourths of the bar steel of Germany. Probably the straight rolling mills do not produce over one seventh. The straight rolling mills are almost entirely dependent on the large steelworks for their material, and they are at a disadvantage both in the manufacture and sale of light rolled products. The superiority of the steelworks is based on (1) technical superiority, (2) economy in general expenses, and (3) economy in freights. Their technical superiority relates almost entirely to standard commodities, produced in great quantities, and is found chiefly in the economy of fuel and in the economy of construction and operation of plant. Considering these economies only so far as they relate to the rolling of the light products, the straight rolling mills concede that the large works have an advantage of from 4 to 6 marks per ton in rolling crude steel. It is principally a question of saving heat by direct rolling. It is also obvious that the construction of a plant for a continuous and uninterrupted process is more economical. This factor, as well as that of saving in general expenses, which is equally obvious, is difficult to estimate. The saving in freight is estimated to average 1½

marks per ton. Not all the large steelworks enjoy these advantages, as they have not all been rationally located and constructed. The commercial advantage of the mixed work rests partly on their commercial and financial preponderance, and partly on their influence over prices and production.

The complaints of the straight rolling mills may be concisely formulated as follows: that the prices of half products are too high in comparison with the prices of light rolled products; that the steelworks, although they control the export, have been dumping half products; that the export of prices are excessively low; and that the export bounties are insufficient to enable the straight rolling mills to compete with foreign mills using German half products. Regarding the price policy in the domestic markets, extensive comparisons might be made; but it is sufficient to cite that of Springmann, a leader of the straight rolling mill group, who divides the decade 1895 to 1905 into two five-year periods, — a period of prosperity and a period of depression. The margin between crude ingots and bar steel in the first period was 49.75 m., and in the second 29.54 m. He compares these with the margins between crude ingots and beams, which for the same periods were, respectively, 21.15 m. and 26.60 m., and he claims that the steadiness of the latter was due to the fact that the steelworks combinations controlled the prices of beams. A representative of the steelworks claimed, on the other hand, that the margins for beams were reasonable, as well as the margin for bars during the second period, but that the margins for bars had been too high in the first period. On a previous occasion Springmann claimed that a margin of 37.50 m. was necessary between rolled ingots (blooms) and bar steel, while A. Kirdorf (head of the Half Products Syndicate) asserted that 22.50 m. was sufficient. The truth here probably lies near the mean. The rolling mills seem to make a better *prima facie* case in the margins for rods. They cite the cost of rolling rods as given by the Half Products Syndicate as 21 m. The price of billets was 90 m., which, together with 21 m. for rolling and 1.50 m. for freight, makes a total of 112.50 m. The prevailing price for rods, including domestic and export trade and deducting bounties, was 108.21 m. from January to March,

1904, and 107.71 m. from April to June, 1904. They were compelled, therefore, to sell at 4.29 m. and 4.79 m., respectively, below a fair cost of production. The representatives of the straight rolling mills claimed that the steelworks made exorbitant profits on half products; but A. Kirdorf denied it, and offered to prove it from the books of his company. He said that there were great differences in cost, and that the steelworks that produced at a disadvantage had as good a claim to have prices adjusted to make their business profitable as the straight rolling mills.

This conflict of interest has not appeared in Silesia, which is due partly to technical conditions and partly to the organization of the industry. A sliding scale has been established between rolled products and pig iron which automatically adjusts the margin.

The Steel Syndicate is incomplete in two important points: (1) the open hearth mills are not in the combination, (2) the B-Products are not syndicated. The bar steel production from the open hearth furnaces is said to be 10 per cent of the total. The Steel Syndicate has made strenuous efforts to bring them in, but without success. It is said that they demand exorbitant quotas. It has also been active in trying to bring about some *modus vivendi* for the straight rolling mills, which can hardly be brought into the syndicate before the open hearth furnaces. Various schemes have been proposed. Under their present disadvantageous position they have a relatively depreciated value. If they were admitted into the syndicate with reasonable quotas, they would unquestionably be coveted by the large mills, but it is difficult to see how the syndicate works could be induced to give away valuable privileges without a consideration. The straight rolling mills have proposed a sliding scale, but the proposed margins are high. Finally, the syndicate has made a counter-proposal that the straight rolling mills buy half products at ruling prices, and sell the rolled products to the syndicate with a fair allowance for the cost of rolling. The syndicate wished to get control of the sale. The syndicate has made some effort to help bring about a separate cartell in bar steel, but the game of cartell politics is complicated, and there were some

reasons for going slowly; *e.g.* securing first the adhesion of the other Silesian mills and the open hearth furnaces. The straight rolling mills, according to admissions from their own side, have been quite immoderate in their demands. Accusations have not been wanting, however, that the Syndicate is really aiming to destroy the straight rolling mills, and to get control of the finished products, though this is emphatically denied.

The complaints of the straight rolling mills regarding the export policy of the Steel Syndicate concerns a matter of much greater interest to German industry and the world at large. The imports of steel are of minor consequence, although in the boom period, especially in 1899 and 1900, there was a considerable importation of pig iron and half products. The exports are shown in the following table:

EXPORTS OF THE GERMAN CUSTOMS UNION[1]

Year	Pig Iron	Half Products	Finished Products
1898	272	35	1312
1899	235	23	1244
1900	191	34	1355
1901	304	202	1815
1902	516	636	2127
1903	418	638	2281
1904	226	396	2022

The domestic demand was so keen in 1899 and 1900 that the exports of pig iron declined. It is remarkable that finished products declined so. With the beginning of the depression in the domestic markets producers were led to increase their exports. This is especially marked for pig iron in 1901 and for half products in 1902. The exports of finished products do not show such a decided increase. The straight rolling mills complained that the steelworks were dumping their production in England, both during the régime of the Half Products Syndicate and since the Steel Syndicate was formed. In answer to this charge the Steel Syndicate submitted the following table for domestic and export sales of half products (finished weights):

Year	Domestic	Per Cent	Export	Per Cent
1902–03	737,121 tons	50.50	723,016 tons	47.97
1903–04	844,629 tons	58.26	605,069 tons	41.47
1904–05	1,018,277 tons	72.12	393,626 tons	27.88

[1] In thousands of tons: thus 272 = 272,000 tons.

The sales in 1904–1905 were made during the régime of the Steel Syndicate. The question of dumping applies only to half products, so far as other branches of the steel industry are affected, because the other A-Products — namely, rails and beams, etc. — are necessarily sold to the consumers in the countries where they are used. National interest, however, is almost equally opposed to dumping these products. The policy of the Steel Syndicate in the sale of all A-Products for the first year of its activity (1904–1905) is shown in the following statement (crude steel weights):

Commodity	Domestic	Per Cent	Export	Per Cent
Half Products	1,154,910	72.20	444,688	27.80
Railway Material	1,049,454	75.25	345,169	24.75
Structural Iron	1,174,147	76.77	355,288	33.23

The Steel Syndicate makes unquestionably a favorable showing. It also points out that, though the export of manufactures of half products has declined somewhat, the decline has not been so great as the decline of half products. It is improbable that the straight rolling mills could have so increased their output as to have absorbed all the half products exported, if they had been given the chance. The straight rolling mills complain particularly of the exports to England. Although the Steel Syndicate could show from the official trade statistics there had been a heavy decline in this particular direction, it was well known that in former years a good deal of the English export was reshipped to America, and so a real decline for the English market was not proven. The best argument of the syndicate was that the German half products did not constitute more than 3.8 per cent of the total English consumption.

The complaints against the export policy of the steelworks were directed against prices quite as much as quantities. Low export prices have always prevailed in the German iron and steel trade. The reports of the German steel companies frequently admit it. There is no question that the export prices of half products have been very low, but various circumstances must be taken into account in estimating the effects. A good deal depends at what point of delivery or sale the prices are compared,

and how the freight is reckoned in making comparisons. The rolling mills are apt to compare prices at the producing mills, while the steelworks prefer to compare the prices delivered at the respective places of consumption.[1] Where export bounties are allowed, they must of course be counted in. In order to discuss this question satisfactorily, it would be necessary to know what the export prices really were, for what quantities they applied, and what proportions of the products made therefrom went to different markets where they really met German competition. The theoretical considerations are intricate, while the information as to the facts is totally inadequate, so that it is impossible to make a very confident statement about the real effects of the low export prices. Lippert, a representative of the straight rolling mills, quoted export prices at Antwerp, f. o. b., at 68 m. for ingots, 72 m. for billets, and 72.50 m. for sheet bars as compared with domestic prices of 82.50 m., 90 m., and 92.50 m. respectively. These were emphatically declared by the representatives to be exceptional, if made in fact; and that this was before the present syndicate was established. Schaltenbrand, one of the directors, asserted that the export was necessary, and they had to take what they could get. He admitted that the export prices were a little lower than the domestic prices, but he claimed that, if account were taken of the export bounties and other conditions, the domestic mills received the more favorable terms. He also quoted the real average proceeds from the export trade of the Steel Syndicate for ingots, billets, and sheet bars; but these figures were not printed in the published protocol. Complaints against the steelworks have also been made with respect to the prices at which they sold finished products

[1] Two calculations may be given for illustration, which were offered at the Enquete concerning the Half Products Syndicate. A. Kirdorf gave the following example. Export price for rolled ingots at works to English mills, 76 m.; freight to seacoast, 3 m.; sea freight, 6 m.; total cost, c. i. f. England, 85 m. Domestic price, delivered, 84 m.; export bounty, 10 m.; total cost, delivered, 74 m. Kirdorf figured for each concern delivered. The German concern which exported its finished product to England still had freight to pay. Springmann made his calculation as follows: Export price for billets, f. o. b. Antwerp, 72 m.; freight from Dortmund (producing works), 5.70 m.; net price at works, 66 m. approx. Domestic price, 90 m.; export bounty, 10 m.; net price at works, 80 m. Springmann figured the price at producing works. *Enquete*, VI., pp. 426, 430.

abroad in competition with the domestic consumers of their half products.

Space does not permit going into further details in regard to this question. It has become chiefly of historical interest in consequence of the recent vigorous *hausse* in the German steel market, which has resulted in the advance of prices all around and brought the export prices, according to market reports, very close to the domestic prices.

In order to equalize the disadvantage at which the German export industry has been placed with respect to manufactured products in consequence of the low export prices of the raw material cartells, export bounties have been paid from time to time by the latter to such of their customers as were engaged in the export trade. This practice extends back to 1891 in the iron trade, and perhaps earlier. The significance of the export bounty system naturally became much greater in the period of depression which followed the crisis of 1900, and it was considerably extended. In 1902 it was systematically organized by the establishment of an "Export Accounting Office" (*Abrechnungsstelle für die Ausfuhr*), in which the coal, coke, pig iron, half products and beam cartells united to pay export bounties to each other, and to the mills which made and exported the finer products. These bounties were based on a calculation of the amount of raw material consumed in making the finished product. The general principles established for the payment of these bounties were, first, that they were payable only to members of a cartell, and, second, that the raw materials consumed must be supplied exclusively by the cartells paying the bounties. At the beginning of 1904, when the Steel Syndicate commenced operations, the bounties were paid according to the following scale:

1.50 m. per ton of coal.
2.50 m. per ton of iron (exclusive coal bounty).
15.00 m. per ton of half products (inclusive coal and iron bounty).
20.00 m. per ton of structural steel (inclusive coal and iron bounty).

Except for a slight reduction of the bounty on half products for a short time these bounties prevailed through 1904 and 1905. At the end of 1905 the Steel Syndicate decided to grant export

bounties only to such cartells as syndicated the foreign as well as the domestic sales, but at the same time they made a very important exception to this, as well as their previous rule; namely, they consented to give a bounty of 7 m. per ton for half products consumed by the producers of steel bars, although there was no cartell at all in this commodity. This bounty was to begin with the second quarter of 1906. The reason for this exception was that the establishment of a cartell in bars was deemed practically impossible. If, as has been frequently claimed, there are some influential steelworks in the syndicate who have obstructed the formation of a cartell for bars, this measure seems calculated to bring them around somewhat.

In the agreement constituting the Steel Syndicate one of the powers of the Beirat is "the granting of authority to the Vorstand to conclude protective and other agreements." Under this clause the syndicate has made agreements with foreign steel producers, which form a cardinal feature in its policy. Such agreements are by no means an innovation. An international rail pool which existed for a couple of years was dissolved in 1886. In recent years there have been numerous international agreements in the steel trade, as, for example, rails, beams, rods, heavy sheets, wire nails, enamel ware, pig iron, etc. These various cartells include a number of different countries, but particularly Germany's nearest neighbors, France, Belgium, and Austria. The policy of forming international agreements is the logical development of the policy of forming local or domestic agreements, and generally presupposes the latter. In the iron and steel industry combinations of a more or less comprehensive character exist in all the important producing countries, and there is no doubt that the formation of powerful combinations in one country stimulates its rivals to strengthen themselves in a similar manner. To a certain extent, indeed, the formation of the United States Steel Corporation has had an influence in bringing about the formation of the Steel Syndicate in Germany. The establishment of the Steel Syndicate not only gave the German producers a greater power and prestige in foreign markets, but it also made it possible for them to make advantageous agreements with their rivals for the elimination of compe-

tition. The Steel Syndicate promptly availed itself of this opportunity.

A very circumstantial account of certain of these transactions was published in the *Revue économique internationale* for December, 1904, signed by "un industriel belge." According to this authority a meeting was held at Aix-la-Chapelle in June, 1904, which resulted in the formation of an international beam pool between Germany, Belgium, and France, with quotas of 73.45 per cent, 15.05 per cent, and 11.05 per cent, respectively. This agreement was signed on November 24, 1904. It is to terminate on June 30, 1907. Central selling offices were established at Düsseldorf, Brussels, and Paris. Negotiations were being conducted at the same time concerning the formation of an international rail pool, which appears to have been consummated on November 28, 1904, to take effect from October 11, 1904. The countries entering this pool and their quotas were as follows: England, $53\frac{1}{2}$ per cent; Germany, 28.83 per cent; Belgium, 17.67 per cent; and France (which came in later), $\frac{4.8}{104.8}$ for the first year, $\frac{5.8}{105.8}$ for the second, and $\frac{6.4}{106.4}$ for the third. This agreement was to terminate on March 30, 1908. The central bureau was located in London, besides local bureaus for each national group. Since then the chief American rail producers have joined this international pool. The *Berliner Tageblatt* reported this fact on December 1, 1904, the *Deutsche Industrie-Zeitung* alludes to the fact in its issue for January 20, 1905, (stating that the pool had already received numerous orders), and Kollmann states it also in his account of the Steel Syndicate, giving the American members of the pool as the Steel Corporation, the Lackawanna, and the Pennsylvania.

Information regarding this agreement and the participation of American interests therein was not very generally known outside the trade apparently, so that on July 1, 1905, the New York *Times* came out with headlines announcing that the European and American producers had divided the world's markets, according to which Central and South America were to be left to the United States, together with other details. Various state

ments have appeared concerning the terms of the agreement, but none apparently which bear the evidence of complete and authentic information. An article in the *Neue Hamburger Boersen Halle* which seems to have had some special source of inspiration declares that the terms of the agreement, etc., had been kept secret at the express wish of the Americans; and, in this connection, it may be noted that the directors of the Steel Syndicate refused to discuss or divulge their agreements with foreign producers on the ground that they did not feel authorized to reveal the business secrets of their associates. Considering only the aspects of this situation from a German standpoint, it is evident that such agreements are of great significance to the steel trade, and a benefit not only to the German steel trade, and but also to the whole national economy. For England, which has been the dumping-ground of all nations, the situation is doubtless more complicated; but for Germany it can hardly be disputed that an arrangement that tended to raise export prices more nearly to a level with domestic prices would be of almost unalloyed advantage. For the straight rolling mills an international pool in half products would be particularly beneficial; but, although negotiations in this direction are reported, nothing seems to have been accomplished.

In passing judgment on the Steel Syndicate, it must be borne in mind that it is only a torso until the light rolled products (B-Products) are included in its sales. It is probable that this will be accomplished before long, and it is probable also that the process of concentration will not end at that point. It is possible that something more comprehensive than the United States Steel Corporation, though not as large, may be the final result. According to the prevailing German view of industrial organization, combinations, like men, may be "good" or "bad," according as they conduct themselves. Up to the present the Steel Syndicate should be classed, on the whole, as a "good" combination; but it has yet to endure a serious ordeal, although the present *hausse* may show whether it possesses the most difficult and most valuable of cartell virtues, — moderation.

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