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Fixing Re-Sale Prices

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The Great Atlantic and Pacific Tea Company v. Cream of Wheat Company, 224 Fed. 566.

This decision handed down by Judge Hough of the Federal District Court may be considered interesting as the first that has come to public notice, in which the second section of the Clayton Act has been construed, and as another step in the effort of large manufacturers to control the career of their products after they have left the producers' hands. The Cereal Company had published a sales scheme in which they reserved the right to refuse to sell to any one who would not abide by such requests as they should make. There was no contract for a fixed price, but, taken with the history of their dealing with plaintiff, the scheme meant, in the words of the Court, "Keep up the retail price or we will stop supplying you, if we think such stoppage profitable." The plaintiff, the owner and operator of a large number of "chain stores," brought suit to compel the defendant to supply them with carload lots at wholesale rates, claiming that a refusal would be a violation of Sec. 2 of the Clayton act. This section makes it unlawful to "Directly or indirectly discriminate in price between different purchasers—where the effect is to substantially lessen competition or tend to create a monopoly," but it does not forbid discrimination on account of quantity, or quality, etc., and does not prevent "persons engaged in selling goods, wares and merchandise in commerce from selecting their own customers in bona fide transactions and not in restraint of trade." It may be noted that the Sherman law was not brought into the case by either counsel or the court.

The court held that the plan of the defendant was not such price discrimination as to substantially lessen competition, as it was at most a mere refusal to deal in an article that was not a necessity or even a staple article of trade. In the following quotation the opinion is expressed that Sec. 2 does not apply to defendant at all. "Sec. 2 plainly identifies the lessening of competition with restraint of trade (cf. the body of the Section with the last exception), but price discrimination is only forbidden when it substantially lessens competition. Construing the whole section together, the last exception reads that a vendor may select his own bona fide customers providing the effects of such selection is not to substantially and

unreasonably restrain trade. How it can be called substantial and unreasonable restraint of trade to refuse to deal with a man who avowedly is to use his dealings to injure the vendor, when said vendor makes himself only such an advertisement-begotten article as Cream of Wheat, whose fancy name needs the nursing of carefully handled cereals to maintain an output of trifling moment in the food market—is beyond my comprehension."

The Court adds that such a construction as the plaintiffs desire would cause the law so to operate as to confiscate property for a private purpose and be unconstitutional. But this may be considered as dictum.

Throughout the decision there is a marked tendency to view with disfavor the practice of plaintiff in cutting rates, Judge Hough considering that it injured other dealers without a compensating benefit to the general public; and so strong is this tendency as to suggest the question whether he would not have been willing to enjoin plaintiffs for unfair competition. He says, "In short, it is plaintiff and not defendant that pursues methods whose hardship and injustice have often been judicially commented upon." This view would seem rather extreme.[1]

More recently there has appeared a decision which seems at first sight, at least, to conflict with Judge Hough's rule. The case was that of the United States v. Kellogg Toasted Corn Flake Co. et al.[2] The defendant owned a patent on the boxes in which their product was marketed and printed notices on them that selling below ten cents per package was an infringement of their patent right. The Court enjoined them from publishing this notice and also declared that their sales plan was unlawful under the Sherman law, and enjoined them also against requiring jobbers to make any agreement for a fixed re-sale price and also "from suggesting to said retailers, in writing or otherwise, that if they fail or refuse to observe said fixed price they will be cut off from a further supply of said product." The decree was given by the agreement of the parties. The Cream of Wheat Company had sent out notices whose effect was to suggest directly the very thing which the Court here holds unlawful. It has been suggested, however, that there is no irreconcilable conflict between the decision of the two cases. The

[1]Our attention has been called to the fact that the Tea Co. has now instituted a suit in the New York District Court to have the sales plan of the Cream of Wheat Company declared illegal under the Sherman law.

[2]United States Dist. Court, Eastern Dist. of Mich., Southern Div., Case No. 5570.

object of the Cream of Wheat case was to obtain an injunction under Sections 2 and 16 of the Clayton Law and Judge Hough expressly ruled out any consideration of the Sherman Law, upon which the Kellogg case was decided.

But Judge Hough's reasoning, it would seem, is contrary to the decision in the latter case. He states that restraint of trade has the same meaning in the Clayton Act as in the Sherman Act, and at some length gives as his opinion that the plan of the Cream of Wheat Company was not an unreasonable restraint. It has been noted above that he was inclined to look at the operation of price cutters unfavorably. Since corn flakes and cream of wheat occupy practically the same position in the food market, if the plan of selling the latter is not an unreasonable restraint, the same plan of selling the former would not be unlawful under either the Clayton or the Sherman Act. Besides, Judge Hough expressed the belief that Congress had no power under the Constitution to pass a law authorizing the Court to issue an injunction compelling a producer to supply a retailer with his product. It would seem that this view would be applicable to the decree in the Kellogg case. Do not the following words apply equally to either company and to either law? "If defendant's actual scheme of interstate business is unlawful, the United States certainly, and now perhaps an individual plaintiff, can put it out of business, but neither the nation nor any individual can take away its property with or without compensation for the private use of any one."

As matters stand neither case can be taken directly to the Supreme Court and it may be years before this precise point will be ruled upon; meanwhile, the question of price fixing is one that commands a good deal of interest. It seems that an express contract between the manufacturer of an unpatented article and the wholesaler fixing the re-sale price is invalid.[3] Also the publisher of a copyrighted book cannot by a notice in the book establish a minimum price and treat as an infringement of the copyright a sale below that price.[4] A producer of a patented article cannot enforce under his patent right a fixed re-sale price, by printing on the package containing the article a notice that selling below such price is an infringement, and also adding that the notice is a condition of the contract of sale to the retailer and that all rights

[3]Dr. Miles Medical Co. v. Park Co., 220 U. S. 373.
[4]Bobbs-Merrill Co. v. Straus, 210 U. S. 339.

revert to the patentee on the breach of the condition.[5] The ground of the decision was that with the sale the rights granted by the patent laws were exhausted and the article passed beyond the patent monopoly. The same conclusion was reached where in a similar notice it was provided that the title should remain in the manufacturer until the expiration of the patent having the longest time to run and then to go to the purchaser only if all conditions had been complied with, the Court holding that as a sale was the ultimate purpose the temporary reservation of title was not sufficient to take the case out of the rule laid down in the Bauer case above.[6] On the other hand, the patentee may assign his exclusive right to make the article on condition that the assignee will maintain a certain price.[7]

These cases would seem to make an agreement for a certain minimum price on patented articles unlawful, but in a recent decision Judge Geiger drew a distinction between such agreements and the circumstances governed by the Bauer case, limiting the latter to cases where the reservation of rights under the patent laws was attempted by a notice and holding good the same reservation obtained by an express contract.[8] It is regrettable that the learned Judge did not express more clearly the reasons for the distinction. As the Miles case above decided that similar contracts regarding unpatented articles were void, it would seem that the basis of the decision must be some right derived from the fact that the article was patented. Yet if a condition in the sale to the retailer fixing the re-sale price expressed in the form of a notice cannot be upheld upon this right, it is not clear how a contract to the same effect can be based upon it. A case similar to this one was differently decided by Judge Hollister, who held that as the sale took the article out of the patent monopoly a contract fixing a re-sale price was void under the rule in the Miles case.[9] The learned Judge also drew a distinction between an actual sale of the article and an assignment of the exclusive right to sell granted by the patent law. It is conceived that this is the distinction between this and the Bement v. Harrow Company case above, where the exclusive right to make was assigned.

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[5]Bauer v. O'Donnell, 229 U. S. 1. United States v. Kellogg Co., 222 Fed. 725. The latter case is the same as the one commented upon above. The opinion is on a motion to strike out and is concerned only with the rights under the patent laws.

[6]Victor Co. v. Straus, 222 Fed 524.

[7]Bement v. Harrow Co., 186 U. S. 70.

[8]American Graphophone Co. v. Boston Store, 225 Fed. 785

[9]Ford Motor Car Co. v. Union Motor Sales Co., 225 Fed. 373.

The owners of various patents which are used in the manufacture of one article, but which are complementary to each other, and are upon devices to be used in different portions of the process of manufacture may legally combine to protect and obtain the benefit of their patents. United States v. United Shoe Machinery Company, 222 Fed. 349. But this right is to combine only for the protection of the patents. If they are on devices which are designed to perform the same service, and if the effect of the combination is more than protection of the patents and extends to monopoly through unreasonable restraint of trade, flowing directly from the agreement, it constitutes a conspiracy in restraint of trade and is illegal. Standard Sanitary Manufacturing Co. v. United States, 226 U. S. 20. United States v. Motion Picture Patents Company, 225 Fed. 800.

There is a bill before Congress making it a felony to cut prices and one to establish the legality of fixing prices. Bills introduced into the Legislatures of New York and other states forbid the fixing of a re-sale price. Several concerns with large resources have taken up the practice of distributing their goods on genuine consignment contracts, keeping the entire title in themselves until the sale to the consumer is made. This ties up much capital and is possible only to large firms.

The Cream of Wheat case may point out another possible way in which prices may be to some extent legally regulated. Because an agreement to fix prices is illegal, it does not necessarily follow that there are not lawful means by which the same object may not be partially, at least, enforced. Under this decision a producer may by a careful selection of customers obtain as his distributing agents only men who will voluntarily accede to the wishes of the producer. The distinction between an agreement to sell above a certain minimum price and the refusal to deal with those who are unwilling to do so, may seem over nice in view of the fact that retailers may be virtually compelled by the demands of their customers to keep certain goods in stock. This case, however, is limited in its reasoning to such commodities as Cream of Wheat, which are not "necessities of life, or even a staple article of trade," leaving undecided whether in regard to the more necessary articles the same method of business would be lawful or not. It may be that the Court considered this to be the test whereby it could be determined whether or not the case fell within the act. This view, of course, depends upon whether the Kellogg case above is followed or not. If under that case such restraints of trade are unreasonable this plan could not be worked. But if Judge Hough is upheld in his opinion either that such

methods are legitimate, or that a law compelling the producer to supply a retailer is unconstitutional, this plan may be feasible.

Price cutters argue that they benefit the community by supplying goods at low prices. Their opponents urge that the benefits of such methods of competition are limited and temporary; that their theory is that on which the Sherman law was passed; to prevent cheap selling where there is competition, and dear where there is none. Whatever may be the final solution, the question is one that concerns the entire public, the producers, the retailer and the consumer, not only those who are so situated as to take advantage of cut prices, but those who cannot do so. It is not against public policy to allow a reasonable profit, but it is against public policy to allow an unreasonable and monopolistic profit or to depress sales, so as to hamper legitimate business or to create a cut-throat competition.

S. McK.

(Since the above note was written Judge Lacombe for the Federal Circuit Court of Appeals, on November 10th, sustained the decision of Judge Hough in the Cream of Wheat case. Attention is called to the fact that the sales of the company amount to only one per cent of the total sales of the wheat in question, and to the "elementary law" that a trader may select his own customers.—Ed.)