Trade Association Information Exchanges Under the Anti-Trust Laws: Compulsory or Open Competition

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•PERHAPS the most spectacular recent development in consent decrees involving information exchanges has been in the direction of compelling the exchange of information of a quite different kind than has been usual in the past. This is probably symptomatic of the oligopolistic conditions now prevailing in many of our major industries. Thus, the government recently worked out a consent decree against General Electric which proposed, among other things, that the price of each component of a total bid on a job be itemized and made available to all other firms in the industry. This novel provision was proposed on the theory that such information might enable a smaller firm to compete for part of a large contract by bidding the low price on individual parts. Actually, the government succeeded only in inserting provisions against refusing to sell circuit breakers to any firm which might in turn sell them to manufacturers of equipment in which they would be incorporated and in authorizing a kind of joint bidding which would be helpful to smaller firms.

The need for these provisions in a consent decree so underscores what has happened in American industry that it can well serve as a point of departure from which to survey the past six or seven decades of development under the anti-trust laws, particularly as they relate to information exchanges.

I propose to examine such examples as they have related to price fixing in the following sequence: (a) starting with the Addyston Case in 1898; (b) then at the phenomenon of delivered pricing as a method of price fixing based on information exchanges; (c) next at the so-called "open price" developments which were initiated by the lumber interests in the 1920's; (d) then at the consent decrees which would interfere with the exchange of cost information; (e) then at the present G. E.-Westinghouse price conspiracy and some of the novel provisions which the Department of Justice sought to include in a consent decree against G. E.; and (f) finally at recent proposals for remedial action which might get us off the horns of the dilemma which we find ourselves in, which compels us on the one hand to break up price-fixing schemes in the nonregulated industries and then immediately counter with decrees which seek to deter the giants of an industry from competing too vigorously on a price basis so as to destroy the marginal producer protected by the illegal price-fixing schemes.

THE ADDYSTON CASE[1]

In the 1890's a trade association known as the Southern Associated Pipe Works was developed as a vehicle for price rigging and market allocation by the industry. The information exchanged consisted of data necessary for a scheme in which (a) certain cities were reserved for sales by designated members of the association; and (b) bids were set on jobs in the remainder of the territory by an association with the member getting the right to low bid who was willing to put the highest portion of profit into a

[1] United States v. Addyston Pipe & Steel Co., 85 Fed. 271 (C. A. 6, 1898).

Paper presented at the Third Annual Workshop on Highway Law, Louisiana State University, April 13-17, 1964.

kitty, for division on the basis of capacity, among association members. The purpose was alleged by the association to be to avoid ruinous competition and to allocate a fair share of the work at such reasonable prices as would enable all members of the industry to continue in business. The purpose proved by the Government was to hold, by agreement, prices at levels such as to make it unprofitable for producers outside "pay territory," as it was termed, to compete.

This was a relatively simple scheme based on the notion that pipe would not come into "pay territory" under the cost of production plus freight. These were little recognition of the effect of fixed and variable costs pursuant to which, if in fact any contribution could be recovered on such fixed costs, freight would be absorbed and pipe shipped in. But in the reserved cities, far from outside competitors, the effect of the agreement was to eliminate by agreement nearby competition which could absorb freight and still enhance total profit per ton. The exchange of information allegedly to avoid ruinous competition was a price-fixing and market-rigging scheme, and illegal per se under Section 1 of the Sherman Act.

DELIVERED PRICING: PITTSBURGH PLUS AND MULTIPLE BASING-POINT SYSTEMS

In the steel industry, price fixing centered around the use of basing point systems. These involved extensive exchanges of information as to railroad rates since the system of price fixing revolved around a base price for steel in Pittsburgh plus railroad freight from this point. This enabled the then dominant Pittsburgh producers to enter any market which they chose. At the same time all other producers eliminated price competition among themselves. Even though inefficient producers could not meet the Pittsburgh price cost-wise, they were able to take a market share because of the "phantom freight" from Pittsburgh to points which might be much nearer to them than Pittsburgh would give them a margin which could absorb the additional cost of the inefficient producer and still leave a profit. They would not be encouraged to expand production, however, since Pittsburgh prices were based on an efficient producer which could cut its prices to keep other producers in line. "Place economy" was thus effectively defeated. In the South, U. S. Steel acquired the Tennessee Coal and Iron properties and directly controlled their pricing and development.

With the outlawing of "Pittsburgh plus" pricing in 1924, multiple basing-point pricing was developed, permitting less dominance by Pittsburgh producers but still preserving price inflexibility. While market allocation or sharing directly was not permitted under the Sherman Act, as demonstrated by the Addyston case, multiple basing-point systems nonetheless achieved some degree of market allocation by assigning basing point mills throughout the country which all producers could quote prices from, plus freight, whenever a customer was closest to the mill.[2] This resulted in uniformity

[2]An abstract of the bids for 6,000 barrels of cement to the United States Engineer Office at Tucumcari, New Mexico, opened April 23, 1936, shows the following:

Name of Bidder	Bid Price per Barrel
Monarch	$3.286854
Ash Grove	3.286854
Lehigh	3.286854
Southwestern	3.286854
U. S. Portland Cement Co.	3.286854
Oklahoma	3.286854
Consolidated	3.286854
Trinity	3.286854
Lone Star	3.286854
Universal	3.286854
Colorado	3.286854

All bids subject to 10 cents per barrel discount for payment in 15 days. (com. Ex. 175-A). See 157 F.2d 576.

of price quotations to the producers but varying returns to producers depending on where they were located vis-a-vis the purchaser. The market could be reached by any producer who was willing to absorb the additional freight charge, and he would absorb freight if he needed the production badly enough, and if the price received would leave something after freight charges to apply to his fixed charges. If he did not, the sales would presumbably go to those to whom they were most profitable on the basis of customer allocation. The Cement Institute Case[3] in 1948 spelled the beginning of the end for the multiple basing-point system and its facilities for fixing prices, market sharing and enforcement.

"OPEN" COMPETITION

Where an industry had no dominant members who could set a price and make it stick because of potential ability to undersell competitors in any market, the trade association information exchange became a far more important factor. Exchange or circulation of freight charges from various points of basing were not enough to secure uniformity of pricing in such an industry.

Such circumstances prevailed in the lumber industry in the early decades of the century, and the "open competition" plan of the American Hardwood Manufacturers' Association came into being as an attempt to deal with competition which was proving too vigorous. The plan was brought to the Supreme Court for scrutiny in a Government suit for injunction in 1921. Because it involved not only the reporting and exchange of past transactions including costs, but also projections of demand into the future, with strong suggestions for curtailing production as a cure to oversupply, it was held to be an unlawful restraint of trade and enjoined.

Thereafter another segment of the lumber industry came up with a plan which deleted all attempts to project exchanged data on costs and supplies into the future or to in any way persuade members as to future programming of prices or production. Despite the protests by the Government that this too was an attempt to stabilize prices by conspiracy, the decree against the association's activities was dissolved by the United States Supreme Court.

Thus a plan of statistical reporting and disseminating was approved which, while involving no coercion, could in fact be used to "suggest" standard prices. Basically, the plan consisted of determining an average industry "cost" for flooring plus a suggested percent on the value of the plant. If such suggested cost, plus a uniform margin of profit, was adhered to as price by the industry, it is obvious that the plan could achieve standard prices for the industry. Combined with basing-point delivered pricing using uniform railroad freight rates, it could eliminate variations arising from the fact that some purchasers might have more economical transportation available to them.

As a result of this validation of information exchanges as to past transactions and past costs, such activities grew and prospered. Only where they were coupled with agreements as to price has either the Department of Justice or the Federal Trade Commission been successful in enjoining them. Nor has the Federal Trade Commission been successful in attempts to stop such exchanges under its broad powers to suppress "methods of unfair competition." Seemingly, standing by themselves, exchanges of past information continue to be valid. However clearly they may be a factor in the stabilization of prices, they are not yet an unreasonable restraint of trade.

Some years ago, however, the Department of Justice did succeed in inserting in a consent decree against a trade association and its members provisions precluding exchange of cost information and circulation of average costs. But these provisions were ancillary to portions of the decree addressed to forbidding participation in a combination or conspiracy as to fixing or maintaining prices or to using any means, including trade association activity, to exact adherence to price-fixing schemes and might not have been obtained by themselves.

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[3] Federal Trade Commission v. Cement Institute, 333 U. S. 683 (1948).

THE GENERAL ELECTRIC-WESTINGHOUSE "EXCHANGES"

An aspect of behind the scenes trade association activity which had reluctantly enjoyed the spotlight in the Addyston case in 1890's, and in the 1920's and 1940's in the Trenton Potteries, U. S. Steel, and Cement Institute cases, came again into the public eye in the late 1950's and early 1960's in what has been called "The Great Price Conspiracy" in the electrical industry.[4]

At "off the floor" gatherings of industry leaders attending meetings of such organizations as the Edison Electrical Institute, the National Electrical Manufacturers' Association, and the Heat Exchange Institute, "exchanges" were going on with respect to allocation of markets and price maintenance—exchanges between competitors which ran squarely into the prohibition of Section 1 of the Sherman Act. They were engendered, it seemed, by G. E. charges that Westinghouse was trying to get a larger share of the available market through price cutting. Despite directives from the top, ostensibly ordering compliance with the anti-trust laws, men in lower echelons engaged in what have come to be known as "the phases of the moon conspiracies," so named because the lunar changes were relied upon to program and pace price rigging engaged in by the conspirators.

One commentator has summarized the procedure at a typical "information exchange" somewhat as follows:

> There would first be a discussion of previous jobs awarded and particularly whether there had been respect by other conspirators for the designated low bidder on the job. These discussions were quaintly designated as "bitching sessions." Discussion would then turn to future jobs, the specifications for which had usually been circulated. Representatives would submit their calculated book prices for jobs and eventually agreement would be reached on a uniform book price for each job. Subject to an overall rotation scheme, allocation of bid positions would be made on the basis of manufacturer arguments as to their qualifications for the job or simply by the drawing of lots for low position if agreement could not otherwise be reached. Low bids would be fixed at a percentage above low bid.[5]

A cumulative list of sealed bid business was kept so as to check the relative standing of each company with its agreed percentage of total sales, and so as to make sure allocation of upcoming business would be consistent with it. Positions on bids would be rotated and generally controlled by a formula utilizing the phases of the moon to achieve what was called "cyclic rotative positioning." On certain business, G. E. was to get 39 percent, Westinghouse 35 percent, ITE 11 percent, A-C 8 percent, and Federal Pacific 7 percent, reflecting, presumably, respective capacities of each. These activities brought indictment and ultimate convictions under the Sherman Act to some 29 companies and some 52 individuals. Fines aggregating almost $2,000,000 were assessed and seven individuals went to jail for terms of 30 days. And the story is by no means over, since just a month ago (March 1964) trials began which will determine how much of the prices charged during the conspiracy must be returned with damages in private suits under the Clayton Act. In the pilot case now in process, two Philadelphia utilities are seeking some $37,000,000 in damages from G. E., Westinghouse, and several smaller firms.

Interest centers, however, in the consent decree by which the Government seeks to avoid such price-fixing conspiracies for the future. To place G. E. in a compliant frame of mind, the Department of Justic threatened to ask a split-up of G. E. if a

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[4] Herling, J. The Great Conspiracy: The Story of Anti-Trust Violations in the Electrical Industry. New York, David Makay, Inc., 1962.

[5] Ibid., p. 105-106, 129.

satisfactory consent decree could not be worked out. Such a split-up might be possible, of course, on the basis of the Clayton Act approach successfully employed by the Government in the General Motors-Dupont case.

G. E. officials balked at one major provision in the proposed consent decree—a provision that would bar the company from selling at "unreasonably low" prices where there is "a reasonable probability that the effect would be to substantially injure competition or tend to create a monopoly." The Government sought by such a decree to protect the smaller competitors against the effects of deep price-cutting. G. E. officials quite naturally bristled at the idea of being told to "compete vigorously but not too vigorously." This is understandable since their fingers have been severely burned in their efforts to achieve this objective, of not too vigorous competition, by recent convictions. They were asked to hold a price "umbrella" over the industry and thus to protect the less efficient producers, something they would argue they had just been punished for doing. They preferred to shift the burden of proof to the Government through a provision which would prohibit low prices quoted "with the purpose or intent" of stifling competition. The Government would be charged, under such a provision, with proving unlawful intent. It would obviously be much simpler to prove that competitors had been injured and that pricing of G. E. was tending toward a monopoly as would be the Government's task under its proposal.

The pressure to "carve up the market" among the industry was sought to be avoided in part by a new type of "information exchange." The Government proposed that all firms itemize the price of each component making up a total bid so that smaller firms might at least bid on parts of a contract even though unable to make a complete bid. Limited point bidding was also authorized, thus permitting smaller manufacturers to bid on at least part of a job.[6]

We have examined the results of anti-trust decrees, based upon full hearing and findings and based upon so-called consent. Each practice dealt with and curbed or outlawed either recurs in slightly different form in the same industries or recurs in

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[6]The following excerpt from a decree in United States v. General Electric Co., Nr. 7058, reported in CCH Trade Regulation Reports (68-55, Dec. 26, 1962), illustrates this approach:

Nothing contained in this Final Judgment shall be deemed to prohibit any of the consenting defendants,

(A) Where in order to sell or offer to sell electrical equipment which included any circuit breaker any person must have an item or items of electrical equipment (i) which it does not itself manufacture, assemble, or purchase from others, (ii) or if it does manufacture or assemble such an item, the item is of such a type or quality that it cannot competitively sell or offer to sell its own item, (iii) or where such person could not singly perform the contract contemplated by such sale or offer to sell:

(1) from formulating or submitting, in combination with any person, a bona fide joint bid or quotation, where such joint bid or quotation is denominated as such or known to the purchaser as such; or

(2) from conducting bona fide negotigations for or entering into any lawful agreement with any person for a bona fide purchase from sale to each other,

(B) Where required directly or indirectly by a governmental agency, from formulating or submitting a combination with any person a bona fide joint bid or quotation which is denominated as such or known to the purchaser to be such;

(C) From entering into, creating, carrying out or implementing by lawful conduct any otherwise lawful contract, agreement, arrangement, understanding, plan or program with any reseller to the sale of any circuit breakers purchased from the defendant, or

(D) From lawfully contracting with any person for the supply to or by such person of any circuit breaker embodying the proprietary design of, or specially designed for, the purchaser upon terms prohibiting the supplier from selling equipment embodying such design to all others (except that the purchaser may authorize sales for repair or replacement purchases).

new industries in the same form. And now, with almost every industry dominated by a handful of firms, even without exchange of information prices may be set without benefit of competition.

Can we get ourselves off the horns of our dilemma? Can we enforce the anti-trust laws against price-fixing and market-sharing in order to protect against exploitation of consumers, without precipitating a situation in which overvigorous competition from the giants in the industry will kill off the competitors and again threaten us with the evils of monopoly?

The proposals of the Government's decree of consent against General Electric provide answers which require a great deal of supervision by the Government to see that they work. Are there other ways available to us which will be more likely to restore the operation of a competitive market and assure us of reasonable prices, efficient allocation of resources, and an appropriate pace of technological progress?

Some argue persuasively that bigness even in an age of automation may not necessarily supply the most efficient producer. Could we require that a showing be made that the size of an industrial unit is justified by "economics of scale," and if such showing is not made, that the unit be reorganized into smaller units? While automation requires large units in most instances, may not some of the alleged savings of bigness turn out to be the ability to come up with a smaller tax bill because of diverse operations, some profitable and some unprofitable, which can be offset against each other? Even in research, may it not be that smaller units, utilizing government and university research facilities to the fullest degree, may do as well; or that research units may successfully operate independently of industry serving large and small on an arm's length fee basis?

Others argue that we have not had a really free economy for a couple of centuries and that reliance upon the marketplace as an efficient allocator of resources and equitable distributor of purchasing power is a fantasy which it is folly to pursue; competitors will inevitably distort legitimate exchanges of information, essential to intelligent production, into devices for price-fixing and market-sharing. This being so, it is suggested that our only alternatives are government regulation, including outright government price-fixing.

Our experience with price-fixing in the regulated public utility industries and with business generally during World War II through O. P. A. has hardly been so successful as to make this route attractive. Yet we know that monopolistic or trade-association price activity cannot be relied upon to protect the public interest.

Perhaps progress in the future lies in a direction recently pointed out by Gardiner Means, the economist who charted the development of the modern corporation with Adolph Berle some thirty years ago in the classic work, "The Modern Corporation and Private Property." Means suggested that we devote our efforts to turning the management of our giant corporations from the search for the greatest profit as a goal to the public interest goals of insuring: (a) that price be in reasonable relation to costs; (b) that benefits to labor and to capital arising from production be reasonably related to their respective contributions to production; (c) that as nearly as possible, optimum use of resources be made so that no more of a given resource is used than is necessary for the end product and that combination of resources is used which involves the least cost; and (d) that there be technical progress to reduce costs, improve product and introduce new products. Means suggests that through an "economic performance act" we set up government rewards for management achieving these goals.[7]

[7] Means, G. C. Pricing Power and the Public Interest. New York, Harpers, 1962.