THE SUPREME COURT AND THE SHERMAN ANTI-TRUST ACT.

"Public policy," Justice Burrough laconically remarked, "is an unruly horse, and once you get astride of him you never know where he will carry you." ¹ But, as is so often the case, the horse is unruly only when abused. When properly managed, he travels the road of sound precept to the goal of justice. And nowhere has this been better illustrated than in the case of monopolies, contracts in restraint of trade, and restrictions upon competition.

The best definition of this "unruly horse" was given by Lord Brougham when he said, "Public policy is that principle of the law which holds that no subject can lawfully do that which has a tendency to be injurious to the public or against public good." ² Now it is obvious that as economic conditions change the standard of what is against public good must change with them. In order therefore to understand the public policy laid down in the Sherman Anti-Trust Act,³ and to be able rightly to interpret that statute, a brief survey of prior economic development in its relation to monopolies, contracts in restraint of trade, and restrictions upon competition, will be necessary.

¹ Richardson v. Mellish, 2 Bing. 229 (1824).
² Egerton v. Brownlow, 4 H. L. Cas. 196 (1853).
I. HISTORICAL DEVELOPMENT OF DOCTRINES AS TO MONOPOLIES, CONTRACTS IN RESTRAINT OF TRADE, AND RESTRICTIONS UPON COMPETITION.

(a) Monopolies.

In early feudal times monopoly, in its broad sense, was everywhere the rule. An incident of the feudal relationship was that the tenant should go only to the lord of the manor for the performance of certain services, and the practices known as forestalling, regrating, and engrossing were common until prohibited by the Statute of 5 and 6 Edward VI (Ch. 14, par. 3). It was not unnatural, therefore, that in later times the sovereign, in order to raise revenue or requite services, should have granted exclusive rights to the use or manufacture of things which were before of common right—a monopoly in the old technical sense of the term—in spite of early legislation against such grants. This practice reached its height in the reign of Queen Elizabeth, when, as Lord Macaulay tells us, "there was scarcely a family in the realm that did not feel itself aggrieved by the oppression and extortion which the abuse naturally caused. Iron, oil, vinegar, coal, lard, tarch, yarn, leather, glass, could be bought only at exorbitant prices."

By the beginning of the seventeenth century the abuse had become so gross that in the famous case of Darcy v. Allein, the court was able to hold that the grant by the crown of the exclusive right to make playing cards within the realm was against public policy and void; and a score of years later the common law, thus established, was re-enforced by the Statute of Monop-
olies, which declared that, with a few exceptions, all monopolies were "altogether contrary to the laws of this realm, and so are and shall be utterly void and of none effect, and in no-wise to be put in use or execution." This rule against the old technical monopolies has been taken by us as a part of our common law, and they have never existed in the United States. It is, therefore, in its broad modern sense that the term is used in the Sherman Anti-Trust Act.

(b) Contracts in Restraint of Trade.

The doctrine against contracts in restraint of trade—using that phrase, as we shall, in its proper common law meaning—was of much earlier origin than the rule against monopolies. It was probably, in part at least, recognized by the Roman Law though it has no place in the law of France. In England the earliest reported case was decided in the reign of Henry V—known as the Dyer's Case. The facts appear to have been that a dyer in connection with the sale of his business bound himself for six months not to exercise his trade in the same town as the plaintiff. So strong was the policy at this time against all contracts in restraint of trade that Judge Hull in refusing to enforce the contract exclaimed, "Per Dieu, if the plaintiff were here, he should go to prison till he had paid a fine to the king." This extreme policy "seems to have originated in certain old laws of England by which no person was allowed to engage in particular kinds of trade or business without first serving a lengthy apprenticeship. It was supposed to be contrary to public policy for a person to bind himself not to engage in a business

* Stat. 21 James I, c. 3.

It should be noted that patents, copyrights, etc., are not true monopolies because the privilege granted is not one that was previously enjoyed as of common right.

A contract in restraint of trade in its technical sense is a contract, ancillary to a principal contract to which the obligor is a party, not to engage in a particular trade, business, or occupation. Cf. Noyes on Intercorporate Relations (2d Ed.), par. 334; 2 Eddy on Combinations, par. 688. Similar contracts not ancillary to a principal contract are always void. Chappell v. Brockway, 21 Wend. (N. Y.) 162 (1839).

Greenhood on Public Policy, 687.

See Rousillon v. Rousillon (1879), L. R. 14 Ch. Div. 351.

for which he had thus become qualified, as the public would be deprived of the benefit of this training and experience in such business, and the tendency of the contract, on account of the prohibition as to other kinds of business, would be to take from him the means of support and reduce him to the position of a pauper." 15 Although the rule continued in all its strictness till the beginning of the seventeenth century, 16 economic conditions were in the meantime undergoing vast changes, and it was becoming apparent that so rigid a doctrine was interfering with every day transactions and was making it impossible for a man adequately to dispose of the good will of his business. Accordingly, before the middle of the seventeenth century contracts in partial restraint of trade—i. e. limited as to time and place—where enforced, 17 and in the leading case of Mitchell v. Reynolds 18 the doctrine was firmly established that contracts in restraint of trade would be upheld if (1) partial and (2) based upon an adequate consideration. It remained, however, for Chief Justice Tindall in the case of Homer v. Graves 19 to lay down the true common law test of the validity of such contracts—i. e.

"whether the restraint is such only as to afford a fair protection to the interest of the party in favour of whom it is given, and not so large as to interfere with the interests of the public. Whatever restraint is larger than the necessary protection of the party, can be of no benefit to either, it can only be oppressive; and if oppressive, it is, in the eye of the law, unreasonable."

Thus the exigencies of the principal contract furnish the standard of reasonableness of the restraining contract. That this test is elastic enough to meet changing economic conditions was illustrated in Nordenfelt v. Maxim-Nordenfelt Co. 20 where, in the case of a world-wide business, a restraint unlimited as to space was upheld.

15 Wright v. Rider, 36 Cal. 342 (1868).
17 Rogers v. Parry, 2 Bulstrode 136 (1635).
18 1 P. Wms. 181—s. c. 1 Smith's Leading Cases 705 (1711).
19 7 Bing. 743 (1831).
20 App. Cas. (1894) 535; 63 L. J. Ch. 908.
While the American courts have not yet applied the above test so as to uphold restraining contracts which are unlimited as to space, the general development of the law of contracts in restraint of trade has been much the same in this country as in England.

(c) Restrictions upon Competition.

Whether or not restrictions upon competition are regarded as against public policy depends upon the answer to the economic question, "Is free competition advantageous?"—Upon this question there is wide divergence of opinion even, as we shall see, among the justices of the United States Supreme Court. In England the judicial view—which in the long run must reflect public opinion—has not been impressed with the value of free competition and accordingly the seeds of the doctrine against the suppression of competition have there usually fallen by the wayside. In the United States, on the other hand, the strong trend of opinion has been in favor of freedom of competition, and the cry has gone up on every side that: "competition is the life of trade." In a general way the test of the legality of a restriction upon competition seems to be its extent—i.e. whether it amounts to a practical control of the market for a useful commodity or for services—while the proper test of the validity of a contract in restraint of trade is its reasonableness. In the case of restrictions upon competition the test of reasonableness is too uncertain as there is no principal contract by which a standard of reasonableness may be fixed. The economic conditions that require rules as to the restriction of competition are comparatively modern, and the origin and development of such rules are entirely distinct from those of doctrine as to contracts in restraint of trade; and furthermore, it is obvious that the tests of legality in the two cases are by no means identical. It is unfortunate, therefore, that the court should have fallen into the way of using the technical words "contracts in restraint

\textsuperscript{21} Wickens v. Evans, 3 Younge & J. 318 (1829); Hare v. L. & N. W. Ry. Co., 2 Johnson & Hemming 8 (1861).

\textsuperscript{22} Cooke on Combinations, par. 118 ff.; Noyes on Intercorporate Relations, par. 352 ff.
of trade” in their broad literal meaning, and, by use of the
syllogism that “competition is the life of trade, therefore every
contract that suppresses competition restrains trade” have ap-
plied them to restrictions upon competition. In some cases this
has led to the error of applying the test of reasonableness to re-
strictions upon competition,23 and seems to have been the cause
of some of the differences of opinion in the United States Supreme
Court as to the interpretation of the Sherman Act.24 The misuse
of these words, has, however, been so frequent in both decisions
and legislation that it now seems impossible to correct it. That
the phrase “restraint of trade” is used in its broad significance in
the Sherman Act and includes restrictions upon competition can-
not be questioned.

II. THE SHERMAN ACT.

The last quarter of the nineteenth century was a time of
great economic upheaval and adjustment to new conditions—an
era of frenzied combination. Everywhere captains of industry
were centralizing and combining their enterprises, and every-
where the cry was going up that competition (“the life of trade”)
was being smothered by combination. The train of popular in-
dignation was laid. The spark only was needed to make it
burst into flame. The formation of the great industrial trusts—
technical trusts from which the whole problem has received its
name—struck that spark, and the flame was not quenched until
Congress passed the Act of July 2, 1890—commonly known as
the Sherman Act or the Anti-Trust Act. Its provisions are too
well known to require detailed repetition here. Suffice it to say,
that it makes criminal (1) every contract, combination or con-
spiracy, in restraint of territorial, interstate, or foreign com-
merce; (2) every monopoly of or attempt to monopolize terri-
torial, interstate or foreign commerce; and that it provides
that the Attorney General of the United States may proceed in

equity for an injunction against infringement of the act, and that those injured by violations of the act may recover treble damages.

We shall now examine briefly the chief cases decided by the United States Supreme Court under this statute.

The first case—commonly known as the Sugar Trust Case—involved the legality of the acquisition by the American Sugar Refining Company—controlling sixty-five per cent of the sugar refined in the United States—of four Philadelphia refineries—controlling thirty-three per cent—stock in the former corporation being given in payment. The court held (Harlan, J. dissent) that the act applied only to transactions which directly affected interstate commerce; that, so far as the record showed, the combination here affected only manufacture; and that commerce was therefore only indirectly affected. While no doubt has ever been thrown on the distinction between commerce and manufacture subsequent cases have greatly diminished the apparent importance of this decision.

In the next case—United States v. The Trans-Missouri Freight Association—the Supreme Court held that a combination of fifteen competing railroads, practically monopolizing the through traffic from the Mississippi and the Missouri to the Pacific, to fix rates by means of a central committee, restricted competition in, and directly affected interstate commerce, and therefore was in restraint of trade and void under the Sherman Act. The two main questions were (1) whether the act applies to railroads and (2) whether it includes reasonable as well as unreasonable restraints of trade. The majority answered both questions in the affirmative, while a strong minority, composed of Justices White, Field, Gray and Shiras, answered both in the negative. The court further held that a combination need not be in form similar to a trust in order to fall within the act.

The following year the same majority held illegal a somewhat similar combination in the case of the United States v. Joint Traffic Associations. The association consisted of thirty-one railroads engaged in transportation between Chicago and the

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* 166 U. S. 290 (1897).
* 171 U. S. 505 (1898).
Atlantic Coast, and its object was to have all changes from established rates emanate from the directors of the companies instead of from the traffic managers. The Supreme Court, however, held that the combination was practically identical with that in the Trans-Missouri Case, reiterated the propositions therein laid down, and held that the act is constitutional under the Commerce Clause.

During the same term the Supreme Court was called upon to determine the validity of the combinations involved in the Live Stock Exchange Cases. The facts in these two cases were almost the same—the main difference being that the members of the Kansas City Exchange were commission merchants while the members of the Traders Exchange purchased and sold cattle for themselves. In each case the rules of the association forbade members from dealing with competing non-members and imposed minor restrictions on the methods of doing business. The court (Harlan, J. dissent) held that the combinations did not directly affect interstate commerce and therefore were not within the act.

At this time it would have appeared to superficial observers that the Supreme Court would apply the Sherman Act to interstate carriers but would never apply it to industrial combinations. It was not long, however, before such persons were undeceived, for the following year the court declared illegal an association of six pipe manufacturers doing business throughout a large part of the United States which they divided into "free" and "pay" territory. In the "free territory" the members competed with each other. In the "pay territory" the price on each contract was fixed by a central committee, and the contract was then given by the association to the member agreeing to pay the largest bonus thereon to the other members, some of whom would usually, for the sake of appearances, be required to submit bids higher than the one agreed upon. That this combination controlled the market throughout a large territory was clearly proved. The court held that the direct effect of the agreement

was to regulate interstate commerce and that the case was therefore not covered by that of the United States v. E. C. Knight Co.

For three years the Supreme Court was not called upon to interpret the Sherman Act. Then in 1902 it held unanimously (three justices taking no part) that the act "clearly does not refer to that kind of a restraint of interstate commerce which may arise from reasonable and legal conditions imposed upon the assignee or licensee of a patent by the owner thereof restricting the terms upon which the article may be used and the price to be demanded therefor." 30

In February, 1904, the Supreme Court, in an action against a western association of tile and mantel dealers for treble damages, reiterated the principles laid down in the Addyston Pipe Case. The association was composed of dealers in tiles in California and of manufacturers in other States, and according to the agreement the manufacturers could sell to outside dealers only at prohibitive prices. The combination controlled the market, and the Supreme Court held that it directly affected interstate commerce and was therefore void.

Up to this point the Supreme Court had laid down the distinction between indirect and direct effects on interstate commerce; and by the standard of the Anti-Trust Act it had judged shameless and undraped combinations both of railroads and industrial plants and had condemned them. But now there was brought before it a combination of competing railroads draped with becoming modesty under the veil of a holding corporation. The Northern Securities Company was to be condemned or acquitted, and in March, 1904, the epoch-making judgment was rendered. 32 The facts are too well known to need repeating. Four justices (Harlan, Brown, Day and McKenna) held that the transaction was in essence a combination; that it directly affected interstate commerce and suppressed competition and was therefore void. On the other hand Chief Justice Fuller and three associate justices (White, Peckham and Holmes) held (1) "that there is no combination in restraint of trade until something

is done with the intent to exclude strangers to the combination from competing with it in some part of the business which it carries on," and (2) that the ownership of stock in competing railroads does not involve interstate commerce. Justice Brewer held the balance of power, and, though he reversed his former opinion that the act applies to reasonable as well as unreasonable restraints, came to the conclusion that the restraint was here unreasonable and tipped the scales against the Northern Securities Company. The decision has never been qualified in any way and is generally accepted as sound both logically and economically.

After reiterating the doctrine that the Anti-Trust Act has no application to contracts not directly affecting interstate commerce, the Supreme Court, in the following year, unanimously declared the Beef Trust an illegal combination. The combination here was among packers controlling six-tenths of the fresh meat supply of the United States. They agreed to bid only in conjunction with each other, to restrict shipments, establish uniform rules of credit, etc., with the intention of monopolizing the trade. The court had no difficulty in holding that the commerce involved was interstate and directly affected by the combination in question.

During the same year the court held that the acquisition of quotations on wheat and their distribution to persons approved, excluding bucket-shops, was not a monopoly or combination to suppress competition, but "simply a restraint on the acquisition for illegal purposes of the fruits of the plaintiff's work." 35

In the following year, 1906, the court rendered its first decision as to the application of the Sherman Act to a contract in reasonable restraint of trade—using that term technically—and unanimously sustained it. The contract was a typical one—the vendor of steamers plying between certain points on the

35 Board of Trade v. Christie Grain and Stock Co., 198 U. S. 236 (1905).
Ohio River agreeing not to operate steamers between those points for five years, and the vendee agreeing to maintain certain rates. In the course of the opinion Justice Holmes said:

"Whatever differences of opinion there may have been with regard to the scope of the act of July 2, 1890, there has been no intimation from any one, we believe, that such a contract, made as part of the sale of a business, and not as a device to control commerce, would fall within the act. On the contrary, it has been suggested repeatedly that such a contract is not within the letter or spirit of the statute."

Two years later the court made it clear in the case of Shawnee Compress Co. v. Anderson that such ancillary contracts would not be sanctioned if in unreasonable restraint of trade. In this case the Shawnee Company leased its property to the Gulf Co. covenanting that it would not "directly or indirectly engage in the compressing of cotton within fifty miles of any plant operated by the tenant." The case, as Justice McKenna said:

"presents something more than the acquisition by the Gulf Co. of another compress—of a mere addition to its business. It presents acts in aid of a scheme of monopoly ............ The principle (that the sale of the good will of a business with an accompanying agreement not to engage in a similar business is valid) is well understood. The restraint upon one of the parties must not be greater than protection to the other party requires."

Two months before the above decision was rendered the Supreme Court, in the Danbury Hatter's Case, held that a combination of laborers to prevent, by means of boycotts, etc., the interstate, as well as the intrastate, transportation of the plaintiff's goods was void under the Sherman Act and allowed recovery of treble damages. The unanimous opinion of the court was rendered by Chief Justice Fuller, who said:

"If the purposes of the combination were, as alleged, to prevent any interstate transportation at all, the fact that the means operated at one end before physical transportation com-

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31 209 U. S. 423 (1908).
32 Loewe v. Lawlor, 208 U. S. 274 (1908).
menced and at the other end after the physical transportation ended was immaterial.

"Nor can the act in question be held inapplicable because defendants were not themselves engaged in interstate commerce. The act made no distinction between classes. It provided that 'every' contract, combination or conspiracy in restraint of trade was illegal."

The latest case decided by the Supreme Court under the Sherman Act involved not so much the illegality of the combination—the Wall Paper Trust—which was evident,—as its right to recover on a contract made in accordance with the terms of the illegal combination. A divided court held that there could be no recovery inasmuch as the contract was "made up, within the knowledge of both seller and buyer, with direct reference to and in execution of certain agreements under which an illegal combination represented by the seller was organized." 39

An examination of these sixteen cases reveals the following facts. First, that the Sherman Act does not apply if interstate commerce is not directly affected. Upon this principle it was held inapplicable in four cases, viz: the Sugar Trust Case, the Live Stock Exchange Cases, and the Barber Asphalt Case. Second, that the Sherman Act does not apply to contracts between a patentee and his licensee restricting commerce in a patented article, or to contracts restricting the distribution of news acquired to such as would make lawful use of it. Upon this principle the contracts were upheld in two cases—viz: the National Harrow Case and Board of Trade v. Christie Co.

Of the remaining ten cases, two—the Cincinnati Packet Case and the Shawnee Compress Case—involved true contracts in restraint of trade, and were decided by in effect applying the common law test of reasonableness. The other eight involved combinations to restrict competition, each of which was condemned by an application of the proper test—i.e. the test of extent.

That the Sherman Act has changed the common law as it

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39 Continental Wall Paper Co. v. Voight and Sons, 212 U.S. 227 (1909); Cf. Connolly v. Union Sewer Pipe Co., 184 U.S. 540, with which the minority held the decision was irreconcilable.
existed in 1890 cannot be doubted, for the common law had confused true contracts in restraint of trade with contracts and combinations to restrict competition, and the courts had often fallen into the error of applying the test of reasonableness to restrictions upon competition. It is submitted, however, that the Sherman Act as interpreted by the Supreme Court, instead of being revolutionary, as so many people have claimed, has, in reality merely corrected an error into which the courts had fallen—the error of confusing restraints of trade with restrictions upon competition. When the court has said that the act applies to reasonable as well as to unreasonable restraints of trade it has, in reality, merely emphasized the fact that the test of reasonableness is not the proper one by which to judge restrictions upon competition. When true restraints of trade have come before it, the court has not hesitated to judge them by the standard of reasonableness.

With regard to the second section of the act it should be noted that "the idea of monopoly is not now confined to a grant of privilege. It is understood to include a condition produced by the acts of mere individuals. Its dominant thought now is, to quote another, 'the notion of exclusiveness or unity', in other words the suppression of competition by the unification of interest or management, or, it may be, through agreement and concert of action. And the purpose is so definitely the control of prices, that monopoly has been defined to be unified tactics with regard to prices." As so used monopoly includes illegal combinations to restrict competition, or in the words of the first section "combinations in restraint of trade or commerce," and it would seem that, as stated by Justice Holmes in his dissenting opinion in the Northern Securities Case:

"all that is added to the first section by section 2 is that the penalties are imposed upon every single person who, without combination, monopolizes or attempts to monopolize commerce among the States, and that the liability is extended to attempting to monopolize any part of such trade or commerce." 41

40 National Cotton Oil Co. v. Texas, 197 U. S. 129 (1905).
41 193 U. S. 197, 404 (1904).
Thus construing the Sherman Act the Supreme Court has declared illegal (1) open combinations to restrict competition among competing interstate carriers (Trans-Missouri Freight Case), (2) open combinations of manufacturers to restrict competition where the effect on interstate commerce is direct (Addyston Pipe Case) and (3) combinations, effected by means of holding companies, to restrict competition among competing interstate carriers (Northern Securities Case). At the present term it will be called upon to decide, in either the Standard Oil Case or the American Tobacco Case, the validity of (4) combinations of manufacturers, effected by means of holding companies, to restrict competition where the effect on interstate commerce is direct. Both combinations have already been declared illegal, the latter by the Circuit Court for the Southern District of New York,\textsuperscript{42} the former by the Circuit Court for the Eastern District of Missouri,\textsuperscript{43} and it seems probable that in both cases the judgment will be affirmed.

If the government is successful in these suits new methods of combination will doubtless be tried. The most obvious of these is the formation of a giant corporation to take over the entire properties of the combining companies which will thereupon go out of existence. Although it is thought by many that such a transaction cannot be differentiated from a \textit{bona fide} sale, in which there is no element of combination, the better view would seem to be that if the transaction is in essence a combination, though veiled under the cloak of a sale of corporate property, it is illegal under the Sherman Act. As stated by Judge Noyes:

"Whether a transaction between corporations or between individuals amounts to a sale or to a combination depends upon whether the vendor actually parts with all interest in the property sold or merely changes the form of the investment. A \textit{bona fide} sale of a plant for cash or its equivalent possesses none of the elements of combination. On the other hand an exchange of one plant for an interest in united plants possesses all the elements of combination. How this exchange is effected is im-

material. An ordinary method is to pay the purchase price in the shares of the corporate combination. Sometimes these shares are delivered to the vendor corporation; sometimes they are distributed directly among its stockholders. It is not material which course is taken. In such a transaction the stockholders—the ultimate owners—stand for their corporation."

The mere fact that the combining corporations go out of existence does not determine that the transaction is not a combination. If a scientific illustration may be pardoned a close analogy might be drawn between such a transaction and the combination of chemical compounds. The combining substances themselves cease to exist and their atoms rearrange themselves to form the resulting substance. A chemical as distinguished from a mere physical combination has taken place but it is none the less a combination.

If a Federal Incorporation Act, such as was recommended by President Taft in his message to Congress on January 7th, 1910, is passed it may well be that the danger of this form of combination will be obviated by provisions for strict federal control, and the act may thus repeal the Sherman Act pro tanto. Until such federal control is secured the dangers in this form of combination are almost as great as in the case of a holding corporation.

One word remains to be said with regard to proposed amendments to the Anti-Trust Act. The one most often agitated is the insertion in section (1) of the word "unreasonable" before the phrase "contracts, combinations, in the form of trust or otherwise, or conspiracy in restraint of trade or commerce." If the position taken in this article be correct the effect of such a change would be to go back to the error into which the common law of 1890 had fallen—i. e. to apply the test of reasonableness to restrictions upon competition. And, furthermore, in the words of President Taft:

"this is to put into the hands of the court a power impossible to exercise on any consistent principle which will insure the uniformity of decision essential to just judgment. It is to thrust upon

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the courts a burden that they have no precedent to enable them to carry, and to give them a power approaching the arbitrary, the abuse of which might involve our whole judicial system in disaster."  

Another proposed amendment, however, merits more serious consideration. The act in its present form forbids all agreements between competing carriers with regard to rates. And yet some co-operation in this respect seems necessary. The result of the decisions in the Trans-Missouri Freight Case and the Joint Traffic Case has been, in some instances at least, the making of "gentlemen's agreements." Such a method of doing business is in many ways undesirable. To remedy this the passage of an Act providing that traffic agreements, when approved by the Interstate Commerce Commission, shall be lawful and enforcible has been suggested. While such an amendment is conservative and for many reasons desirable, it should be remembered that the Sherman Act "has been on the Statute book now for two decades, and the Supreme Court in more than a dozen opinions has construed it in application to various phases of business combinations and in reference to various subjects matter," 45 and that "the value of a statute which is rendered more and more certain in its meaning by a series of decisions of the Supreme Court furnishes a strong reason for leaving the act as it is." 45

Harold Evans.


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45 President Taft's Message to Congress, January 7th, 1910.