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LEGAL OBSTACLES TO BUSINESS TENDENCIES

By W. F. GEPHART

With the development of representative government, business has been increasingly subjected in its organization and operation to statutory direction and control. In the earlier time of kings, emperors, and despots there was an arbitrary control of business, frequently for the benefit of the favorites. This, in the later days of democratic government, has become a control assumedly in the interests of the public and especially for the benefit of the consumer.

Notwithstanding the frequent complaints that are made against legislation which attempts to regulate consumption, there has always been, particularly since the beginning of representative government, more legislation enacted for the purpose of protecting the consumer than the producer. Indeed, any legislation under our democratic forms of government which is of chief interest and value to the producer immediately incurs the suspicion of the public. In an earlier time, when the supply of goods was limited, laws with respect to engrossing, regrating, and fair prices, all had for their purpose the protection of the consumer just as later-day legislation regarding monopolies, public utility rates, pure food, and numerous other laws have been for the same purpose.

This discussion concerns itself primarily with the statutory as distinguished from the common law. Statutory law cannot and should not be prospective as regarding the changing social order. Unfortunately enacted law is often too retrospective. A law should be a rule of social conduct to which the individual members of the social group give voluntary and indeed unconscious obedience. Nor should the courts be continually reading into the statutory law what is not there. The worst kind of tyranny is a judicial tyranny. If the changing social order makes the law obsolete, as is frequently the case, it is for the people, through their representatives, the legislators, to repeal the law and enact new legislation in harmony with the spirit of the times. It is not for the judges of a court to read into and interpret the law according to what may be their own individual ideas of what constitutes social justice.

In order to examine the degree to which statutory law is in harmony with or opposed to business tendencies, certain examples may be taken from the general fields of distribution and production, although equally pertinent cases might be cited from such specific businesses as banking, insurance, and other industrial activities. Distribution is for our purpose to be considered as synonymous with marketing. Production likewise is to be understood to include the direct activities of man on materials which result in wealth. The most striking contrast to the student of industrial history between production and marketing—that is, distribution—is the high degree of efficiency and the rapid advance which has been made in producing goods.

Our system of distribution is yet largely in the ox-cart stage. Indeed, the progress in production has so far exceeded that in marketing or distribution that the benefit of the reduced costs in producing units of goods is largely lost to the consumer because of the high cost of distribution. It is the field of production which has attracted for many years the best intellects so that as compared either with other business activities, such as marketing, finance, or even political and social endeavors, the efficiency of production far outranks all of them. The chief reason for this is to be found in the fact that production is a more simple and definite problem as regards its organization or end. Personal profit-seeking is the goal which attracts and stimulates human interest. Individual ability is easily enlisted and directed. Distribution is much more complex and concerns many more individuals and organizations. Production has had applied to it much scientific research, the increased use of machinery, skilled labor, scientific organizations, and efficient methods not only in the use of material but in the co-ordination of labor and capital.

But it is only comparatively recently that attention has been given to methods of marketing and it will probably be many years, if ever, before our system of distribution is comparable in its efficiency to the productive organization.

Some of the most marked changes in the field of marketing have encountered more or less obstruction from statutory laws. The chain store method of distribution has, for example, called forth legislation in a number of states in an attempt either to outlaw the chain store itself or, through license and tax legisla-

tion, to make its operation much less profitable. Likewise, buying associations and trade associations have either actually run afoul of the law or their members have through fear of the law curtailed their programs in order to avoid the danger of having their action construed as a restraint of trade. This has been true because most of the monopoly laws and those in restraint of trade assumed that any agreement among producers or consumers is for the purpose of controlling price, and therefore, under the statutory law, might be construed as a restraint of trade. This is an assumption that is not always true either in economic theory or in actual fact, since stability in prices may well redound to an increase in trade and a benefit to consumers as well as producers, depending upon the character of the commodity and the activities of the producing trade or the buying associations.

Again the question of price maintenance has long been before the courts of the United States and decisions sometimes of a contradictory character are to be found on this involved question. So far as the statutory or indeed the common law is concerned as regards the question of price maintenance, the underlying principle seems to be that any agreement by manufacturers to maintain or fix prices at which the distributor may sell an article is contrary to public policy, since the result is assumed to be a lessening of competition and, therefore, a restraint of trade.

The manufacturer argues that the chief purpose of a price maintenance policy is to preserve a market for his product on which he has expended large sums in advertising for the purpose of acquainting the public with the merits of the article and creating confidence in it. If the retailer is not thus controlled in his resale price he is often tempted to cut the price in order to stimulate sales and secure a volume of business and thus reduce his overhead costs. In the meantime, the retailer may, when a large market is created, endeavor to substitute another article at a lower price and thus increase his profits. There thus arise several specific aspects of the price maintenance question.

First there is the primary and legal question whether after a retailer has purchased the article he is not free to sell it at any price on the theory that an individual is free to do with his own as he pleases so long as no public injury is inflicted. On the other hand, the manufacturer insists that price maintenance

should be legalized, asserting that the consuming public cannot discriminate regarding the quality of articles and that when he has established a large market for the product beneficial not only to himself but also to the consumer, there is established a right, if not a vested one, which should not be destroyed by price cutting. There is again what might be termed the consumer viewpoint, namely that the consumer should be free to buy when, where, and what he chooses without restrictions either on the part of the manufacturer or influence of the distributor. It may be stated parenthetically that it does not necessarily follow because the article obtains a market that it is the best possible article of its kind. Manifestly, a widely consumed product must have merit to warrant its continued sale, but it need not be the best possible article. Modern advertising does create markets. But it does not follow that because of the advertising a superior article is substituted for an inferior one. Not infrequently it is not a case of either superiority or inferiority of the article sold by advertising, but often simply the substitution of one article for another.

The pertinent questions, therefore, are, should the law give to the manufacturer a quasi-monopoly of the market which he has thus created through advertising, his sales' organization, and in other ways? Should the government by enacted price maintenance legislation thus emphasize the interest of the manufacturer or the distributor or the consumer? Or should it confine its activities, so far as marketing products is concerned, to such legislation as that in the case of pure foods, public utility rates, anti-monopolistic legislation, and laws against unfair trade practices?

During recent years there has been an interesting experiment to control prices by direct governmental action. While present-day governments have shown an unwillingness to grant legal authority to producers to control the price of their products, yet they have, on the other hand, enacted direct legislation and established maximum prices to be charged, as in the case of public utilities, or by other legislation restricted the acts of producers either singly or in associations from agreeing upon any action to control prices on the theory that the widest possible play of competition among producers best conserves the interests of the public.

In addition to this effort of the government to regulate price through control of the producer, interesting experiments have lately been made by the government itself in an effort to control the amount of the product which goes to the market, thus limiting the supply and hence favorably affecting the price. These have been efforts primarily to benefit the producer and not the consumer, in contrast with what has been the usual attitude of the government in matters of this kind. The most notable examples have been in the case of England with its Stevenson Law in regard to rubber, Brazil in connection with coffee, and most recently the United States with its Federal Farm Board.

In the case of England and Brazil the control of price was sought through regulating the supply which was sent to the market. In the United States, the experiment is more direct, since control of price is being sought by direct purchase of a part of the supply. In the case of rubber and coffee the result has been a failure, largely for the reason that the very initial success carried with it promise of failure in that stimulation of production in other countries as well as in the controlling nation was encouraged. This was true because the price originally sought to be established for the producer insured a profit to him and very naturally made for an increased world supply.

It is too soon to pass final judgment on the experiment in the United States, but there are certain fundamental economic principles which cannot be abrogated by our own or any other government. First, if the government accumulates by purchase any considerable supply and thus holds it over the market, uncertainty is created and prices become unstable, for neither producer nor consumer knows when the governmental agency either will place the supply on the market or will go into the market and buy. Second, if the producers of any commodity are guaranteed by the tax-raising power of their governments a profit on their product, each will strive to produce as much as possible and other producers from other fields will be attracted to an economic activity in which profits are guaranteed. Third, if there is not, therefore, as part of such a program some plan of controlling the supply in harmony with the present and prospective demand for the product, failure is almost certain. If a country produces a very large supply of a product—that is, if it has a practical monopoly, and if other nations cannot produce it

and if there are not any substitutes for the article—then a considerable degree of success might be secured by a plan of government-purchasing and price-fixing, provided the price is not so high as to restrict consumption.

There are, therefore, so many conditions attached to the possible success of such a program that we have not as yet had a successful one. In the present era of international markets with so many sources of and demand for basic commodities, with highly developed transportation systems and rapid means of communication, it will be extremely difficult for any one government to very successfully regulate the price of a basic commodity in our highly sensitive world market. However, governmental effort to control prices directly has never been very successful because it is inherently in opposition to the fundamental principles underlying privately organized competitive industrial society, where each seeks to reap as much profit as possible from a favorable market.

If little or no success has attached to the efforts of government to control directly or indirectly the prices of commodities and if governments have not been willing to grant producers the authority to do so, is there, on the other hand, any hope of stabilizing production and thus indirectly bringing about a greater stability in the trend of prices which would eliminate the recurring periods of over-supply with the attendant industrial depression? The greatest single economic and social problem confronting the world is that of better co-ordinating production and consumption. The condition which has brought this need for stabilization is that there has been such an enormous advance in scientific discovery, inventions, business organization and the consequent mechanization of industry that both in the case of raw commodities and many manufactured articles there is an enormous surplus producing capacity in the world. There is this great and keen competition to obtain the market—that is, in periods of prosperity each producer tries to get to the market as many units of the commodity as possible during a period of favorable prices and this leads inevitably to a maladjustment of the supply and the demand. Then too, this co-ordination of production to consumption is also important in connection with the competition for the control of raw commodities. The solution of this problem will be extremely difficult, but anything that con-

tributes to a greater stabilization of production and consequent reduction in the fluctuation of the price level, together with a reduction in the risk of bringing about these gluts in the market, will largely contribute to social and economic welfare. Neither individually nor collectively over long periods does society gain through these alternate periods of booms and depressions. What might be accomplished on a wide scale is indicated in what has already been done in the case of certain industries where large units have been formed and exercise a considerable control over production. However, the law lends no encouragement but rather discouragement to such a procedure; for combinations, nationally or internationally, are tabooed by the law.

Any attempt at stabilization of this character in an earlier period would have been futile: first, because there was not sufficient information on which to base a system of rationalization or stabilization, and second, because the individual producing units were too numerous and too small. Now, however, we have available not only statistics of potential and actual production of the leading nations and the units therein, but also a wealth of information regarding annual consumption. These statistics come not only from various governmental sources but also from trade associations and private agencies and supply, therefore, a wealth of information upon which might be based more intelligent efforts to co-ordinate the productive capacity of the world with the existing consumptive demand. It may be argued that nothing can be done in this direction and that the automatic forces of competition must be left to regulate this situation, bringing about these periods of alternate plenty and scarcity with the concomitant losses individually and nationally to millions of people. Or it may be argued that such a power should not be granted to individual producers lest they exercise it for their own benefit to the detriment of the public. This is similar to the argument which prevailed in an earlier period of railways and public utilities before supervision and regulation of rates by governments. No one, however, would argue today that the situation is not infinitely better under our system of government regulation of railway and public utility rates than in the old days of cutthroat competition with all of its attendant evils.

The two most important obstacles to bringing about greater stabilization of production and hence this greater harmony be-

tween supply of and demand for goods are: first the statutory laws, especially those in the United States. Our nation was founded by those who believed thoroughly in the theory of competition, free contract, and private property. The marvelous and rapid industrial development was believed to result from the free scope given to private initiative, our natural resources, and the native ability of our people. We permitted and encouraged the freest possible play of individual enterprise, even when it meant the exploitation and waste of our natural resources. We are still very largely devoted to this philosophy of unlimited competition and private initiative. Our people are suspicious of any large business enterprise and are ready to enact laws and prosecute any association or combination which seems to restrict competition.

Yet there is little doubt that if there were not these national and international legal and political barriers, the industrialists of the nation and the world would bring about a greater measure of stability in production. Nor would this necessarily be an effort to control price in a manner to exploit the consumer. This would be true not because these industrialists would be actuated by any particular ethical motive to serve the consumer but because it would be, as the industrialists would maintain, good business to preserve a market for a product at a fair price and at a stable price. Producers no more than the consumers are, over long periods of time, benefited by these alternating periods of high prices and low prices. Over a series of years a level of prices, gradually changing as a result of increased consumption and changes in technological processes is much to be preferred both for producers and consumers.

The second obstacle to such a plan of stabilizing production is the strong feeling of nationalism now actuating the people of most countries. One of the many unfortunate products of the World War was the reviving of this spirit of nationalism which had begun somewhat to wane in favor of greater world co-operation. Nevertheless, there is at present more of a will to cooperate among industrialists, nationally and internationally, than is to be found among any other groups. The world is striving to establish a political League of Nations. An Industrial League of Nations might more easily be accomplished and carry with it great promises of good to humanity. But statutory law,

national and international, does not vision co-operation among producers and distributors. The only place where any effort is being made in this direction is in the Soviet Republics and here it is not a voluntary action, encouraged or permitted by the Government, but one emanating from a small governing class and enforced upon both producers and consumers.

Why then do we find this frequent conflict between the law on the one hand and the industrial and social tendencies on the other? Why is law so conservative, so static, and the industrial and social order so radical, so dynamic? Perhaps the chief explanation is to be found in the nature of law. Social experience has long since demonstrated that a law to be an effective rule of human conduct must command voluntary obedience by the members of the social group. The vast majority of laws are not enforced. They do not need to be.

Industrial evolution is always complex and evokes conflict of interests among individuals and especially between social groups. Some are always benefited, others are always injured. For example, the introduction of the factory system meant the passing of the system of household industry and brought with it the problems of child and woman labor, of the sweat shop, long hours, and other attendant evils. It was, however, a long time after the introduction of the factory system before public opinion sufficiently solidified to lead to the enactment of factory legislation, governing the hours of labor, employment of women and children, and sanitary conditions of work. Again railroad legislation in the United States of a simple character began soon after the development of the railroad, but proceeded not nearly so rapidly as railway development and had to do in its early period largely with matters of incorporation. Soon, however, with the rapidly developing railway system, the problem of competition and rates became very complex, but this situation continued for many years before any comprehensive federal legislation was enacted to regulate interstate commerce.

Finally, in 1887, the Interstate Commerce Act was passed. The people of the country yet strongly believed in the principle of the greatest possible competition among the railroads. Mr. Fink, who at that time was President of the Atlantic Steamship and Railway Company, pleaded with Congress to permit pooling, but to Congressmen as well as to the people pooling meant less

competition and there was no sentiment of any importance favoring it. Nevertheless, in 1920, Congress passed an act which encouraged and even commanded the railroads of the United States to consolidate, thus limiting and even abandoning the old theory of encouraging and forcing unlimited competition. It thus took over thirty years for public opinion to comprehend that unregulated competition among railroads was not inherently a virtue of our transportation system. Transportation conditions long before 1920 demand greater unification of the railroad system and indeed it had gone on. But it was chiefly of the type of end-to-end consolidation rather than that of parallel and feeder lines. It would have been useless in an earlier period for any Congressman to suggest that the railways ought to be permitted to form larger systems and indeed many cases in the courts give witness to the fact that the temper of the people would not permit railway consolidations, since consolidation to the public meant monopoly.

All these and other examples that might be cited show that under a competitively organized industrial society and a democratic and representative government, sensitively responsive to the opinion of different social and industrial groups, statutory law will never keep pace with changing industrial and social conditions. No doubt real injury and loss is entailed on society by this necessity of waiting until public opinion is formed on these economic questions before they can be legislated upon. But to enact laws before voluntary obedience would be given to them would mean the destruction of all law and social order, for it must be emphasized again that, under any form of government, the vast majority of the laws cannot and are not intended to be enforced.

What can then be done to bring enacted law into greater harmony with changing industrial and social conditions? The chief reliance must be placed, as in so many other difficult problems which trouble the human race, only in a higher level of intelligence among the people at large. This means in a practical sense that it is a matter of better educational results from our schools and colleges. This situation is especially true among people who have democratic political organizations. If the voter has the wit and wisdom to elect legislators of intelligence, and if both the voter and the legislator have the intelligence to com-

prehend the direction and meaning of the changing industrial and social order, then old laws will be repealed and new laws will be passed not only in harmony with the changed condition, but indeed so as to give direction to the dynamic social and industrial tendencies.

But alas, the underlying forces operating to produce changes in industrial society are so complex and deep that they are largely beyond the understanding of the average voter or legislator until they have fairly well worked themselves out. In purely social institutions, there is another great difficulty in that the average man's opinion of what is proper control of social conduct is very largely a matter of tradition and inheritance. That is to state, a man's idea of the family, of religion, and other basic social institutions is a result of inherited ideas, unconsciously and non-intellectually acquired. He believes about the social order. He learns and knows about the industrial order. For that reason, the social order is much more stable than the industrial. For this reason laws enacted on social matters, passed in times of temporary excitement or under the leadership of demagogues, are the greatest possible failures.

The educational institution to which we must look for relief is largely social in its origin and characteristics. It has, therefore, all the inhibitions which make it slowly responsive to the changing industrial and social conditions and it thus ill prepares the student to understand the industrial, social, and political world and to aid him in devising rules—that is, laws—to govern and direct it.

Progress, whatever that may mean, is painfully slow and achieving it, so far as it ever is achieved, depends largely upon mass ideas and movement. It is only when an idea or a plan wins the support, intellectual or instinctive, of large numbers, that it acquires a momentum and force that makes it effective as a factor in improving the social and political order. The futility of political reforms has been illustrated time and again. Unless the reformers have ideas and plans which secure the permanent support of the people it is but so much misdirected human effort. The numerous reform campaigns in American cities give ample evidence of this statement, for political unconsciousness seems to be the normal state of the average American. His business, his pleasure, and his purely personal affairs are so

much more worth while in commanding his real interest. But, doubtless, the American is no different from the European or even the people of other times. Pericles was under the necessity from time to time of going down to the agora and, assuming the role of a demagogue, appealing to the emotions of the citizens of Athens in order to win support for his plans to wisely govern Athens. There is an enormous amount of static in the social and political order. Industrial society is more dynamic. The reason is not only that there has been a freer play of intellect and reason in the industrial order than in the others, but also that the permanent and personal benefits and gains of being a skeptic and intellectualist in the industrial order are much greater and are usually enjoyed by the individual who has the original thought. If you want to be a Thomas A. Edison or a Henry Ford there is not only no objection or bar to it, but you will probably reap real and personal rewards. But if you insist on being a John Huss or a Christ you will probably be burned at the stake or be crucified.

Hence, we cannot expect that law will be prospective as regards the industrial order and much less so as regards the social order. We can but repeat that enacted law and its interpretation by the judiciary should be a rule of conduct upon which the vast majority of the social group has already agreed. Very properly, the courts should lay great store on the old musty legal tomes and precedent. It is wise for the lawyer and good for society for him to be continually prating about the wisdom of the fathers and the founders of the nation.