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THE AGRICULTURAL COOPERATIVE AND ANTI-TRUST LAWS

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The underlying idea of a cooperative organization is that a business owned by its customers, managed under their direction and having no legitimate loyalties except to them has a better chance to meet their needs than one owned and managed by outsiders. A Cooperative Marketing Association may be defined as a group of producers working together to sell their products without competing against one another.[1]

The legal status of the cooperative form is so vague that it is necessary to examine the relationship between the cooperative and its members, as expressed in its by-laws, articles of incorporation and contractual agreements with its members to decide if it is a "true" cooperative. The four basic principles or cornerstones of the cooperative form of organization are:

> (1) The legally enforceable obligation of the cooperative as a legal entity to return to its member and patrons in proportion to their patronage, all surplus over and above operating expenses.
>
> (2) A membership open to all without discrimination. It follows from this that the value of a share will automatically remain at par and that a transfer of a share of the variable capital of a cooperative will not be an impersonal stock exchange transaction.
>
> (3) The equality of voting rights of all members regardless of number of shares held by the member. This democratic control means that the cooperative is essentially an association of persons and not of capital.
>
> (4) A limited or fixed rate of return on the invested capital so that the cooperative shares are in the nature of an indebtedness and are not entrepreneurial.[2]

While the legislatures and courts of this country have not been uniform in their recognition of these basic distinctions of the cooperative form from other business forms, in this country it may be said that the first, at least, is essential.[3]

The chief uses of the cooperative form in the United States have been:

> (1) Agricultural producers cooperatives, for the sale and processing of produce.

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[1] Vernon A. Mund, Government and Business, p. 218.

[2] Barnes, Cooperatives in International Trade, 1950 Wisconsin Law Review 266.

[3] Charles Bunn, Consumer Cooperatives and Price Fixing Laws, 40 Michigan Law Review 165.

(2) Producers Cooperatives, for the purchase and manufacture of productive equipment and supplies.
(3) Merchant Cooperatives, for the manufacture and purchase of merchandise.
(4) Consumer Cooperatives, for the manufacture, purchase and supply of all kinds of goods and services.[4]

It should be noted, that in the past, there has been a growing tendency toward an integrated cooperative, combining types one and four above, and that until fairly recently, the dominant use of the cooperative type organization has been in the agricultural areas. There are several facts which encourage agricultural cooperative growth. First, the basic American tradition of helping one's neighbor, which is especially strong in the rural area, for example, in the custom of exchanging work and use of machinery, early day "Barn Raisings", etc. Second, the low income of the American farmer,[5] encouraging economy in purchases and maximum return on all sales, which aims the cooperative form seems best suited to serve. Third, is the farmers' distrust and dislike of "big business", even though only local big business. Fourth, the lack of bargaining power of the individual farmer.

Recognizing the need and value of the cooperative form, most states have special legislative provisions for the formation of cooperatives, which although varying greatly in requirements, do provide the legal machinery for creation of such associations or corporations.

The Sherman Anti-Trust Act of 1890[6] expressed the economic policy of free competition, declaring that every restraint of trade and commerce is unlawful. The basic rule of Anti-Trust Legislation, that every unit of the economy should act independently in price determination is in direct conflict with the basic rule of the cooperative, substitution of concerted action for competition in the sale of their produce. The Sherman Act in thus creating a barrier to concerted action in price making made no provision for the exemption or exclusion of cooperatives. Many states, following the lead of Congress, passed similar anti-trust laws. However, the state legislatures, especially those of the agricultural states, were more sensitive to pressure from the Farm Bloc, and many of the early state statutes exempted agricultural cooperatives from their operation. In *Connolly v. Union Sewer Pipe Co.*,[7] the United States Supreme Court held that such an exception, that of Illinois which said:

> The provisions of this act shall not apply to agricultural products or livestock while in the hands of the producer or raiser.

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[4] Note 3, *supra.*

[5] Report of Department of Commerce, "National Income by Industrial Origin", July 1947, showing that even in the current era of farm prosperity, farmers comprising 20% of the national population received only 10% of the national income.

[6] 15 USC, Sec. 1 to 8.

[7] 184 U.S. 540, 22 S. Ct. 431 (1901).

was unconstitutional in that it contravened the equal protection clause of the 14th Amendment of the Federal Constitution.

With this denial of exclusion by the basic Federal law and the Supreme Court's refusal to uphold the exclusion obtained under the state law, Agricultural Cooperatives were faced by the alternatives of openly violating the law or taking steps to change the law, and as violation of the law was prohibitive, their alternatives boiled down to those expressed by Mr. Olds, Chairman of United States Steel Corporation, following the outlawing of the use of the basing point system in the *Cement* case, that the industry is "faced with two alternatives—either to seek remedial legislation or to educate the supreme Court".[8] The Agricultural Cooperative movement, through the Farm Bloc utilized both alternatives.

As to the exclusion by the states of agricultural cooperatives from the operation of their anti-trust laws, there was a gradual erosion of the holding in the *Connolly* case, first by the Court's recognition of the power of the states to authorize farmers to cooperate in marketing their own products in *Liberty Warehouse Co. v. Burley Tobacco Growers Co-operative Marketing Association*,[9] which distinguished the *Connolly* case on the basis of the classification involved, until ultimately in *Tigner v. Texas*,[10] the *Connolly* case was flatly overruled, with Justice Frankfurter stating that it was a proper exercise of legislative discretion based on economic differences between farmer-producers and urban business organizations, that due to the peculiar economic condition of the former, it was a reasonable classification. It should be noted that the Texas statute contained an exclusion for agricultural and livestock cooperatives. Frankfurter stated:

> Since *Connolly's* case was decided, nearly forty years ago, an impressive legislative movement bears witness to general acceptance of the view that the differences between agriculture and industry call for differentiation in the formulation of public policy. The States as well as the United States have sanctioned cooperative action by farmers; have restricted their amenability to the anti-trust laws; have relieved their organizations from taxation.

This clearly indicates the Court's shift of attitude as to public policy, the "education of the Supreme Court" appears complete. That the shift was limited to Agricultural Cooperatives is illustrated by the holding in *Midland Cooperative Wholesale v. Ickes*,[11] where a consumers cooperative[12] sought the protection of the

[8] Journal of Commerce, April 28, 1948.
[9] 276 U.S. 71, 48 S. Ct. 291 (1928).
[10] 310 U.S. 141, 60 S. Ct. 879 (1940).
[11] 125 F. 2d 618 (CCA 8th, 1942).
[12] 15 USC Sec. 833 (i) (13).

Bituminous Coal Act of 1937 which provides that it shall not be an unfair method of competition or a violation of the code to sell to or through a bona-fide and legitimate *farmers'* cooperative organization, the court held that consumer cooperatives did not fall within the provision, and upheld the classification, saying:

> Congress had the right to discriminate between the types of cooperatives and it manifestly did so, and the failure to treat them alike is neither novel nor unreasonable. Laws fostering cooperative marketing and purchasing by farmers have a common genealogy. They stem from a desire on the part of federal and state legislators to extend to farmers ways to enable them to counteract the effects of an increasing urban economy.[13]

The effort by the Farm Bloc for remedial federal legislation first bore fruit in Sec. 6 of the Clayton Act of 1914,[14] which provides:

> Nothing contained in the anti-trust laws shall be construed to forbid the existence and operation of labor, agricultural or horticultural organizations, instituted for the purposes of mutual help, and not having capital stock or conducted for profits, or to forbid or restrain individual members of such organizations from carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held to be illegal combinations or conspiracies in restraint of trade under the anti-trust laws.

Further approval of the cooperative form, at least for the farmer, broadening it to include capital stock, corporate associations and concerted action on selling and pricing was granted in the Capper-Volstead Act of 1922 [15] with this provision:

> Persons engaged in the production of agricultural products as farmers, planters, ranchmen, dairymen, nut or fruit growers may act together, in associations, corporate or otherwise, with or without capital stock, in collectively processing, preparing for market, handling and marketing in interstate and foreign commerce, such products of persons so engaged. Such associations may have marketing agencies in common and such associations and their members may make the necessary contracts and agreements to effect such purposes.

The act stipulated that to come within its provisions, the cooperative must: (1) operate for the mutual benefit of its members, (2) allow each member to have only one vote or limit divi-

[13] *supra.*
[14] 15 USC Sec. 8 *et seq.*
[15] 7 USC Sec. 291, 292.

dends on stock to 8% per year, (3) not deal in products of nonmembers to a greater extent than products of members. The privilege granted of acting in concert with respect to prices was limited to the extent that it must not "unduly enhance" the price by reason thereof, granting the Secretary of Agriculture rather than the Department of Justice the power to scrutinize prices, and empowering him to issue a complaint if the price is "unduly enhanced", and after hearing to issue a cease and desist order if the complaint is justified. This appears to be a very broad exemption from the anti-trust laws for the agricultural cooperative. Congress again smiled upon the agricultural cooperative in 1937, with the Agricultural Marketing Agreement Act,[16] authorizing the Secretary of Agriculture

> to enter into marketing agreements with processors, producers, associations of producers, and others engaged in the handling of any agricultural commodity or product thereof

and then providing that:

> the making of such agreement shall not be held to be in violation of any of the anti-trust laws of the United States, and any such agreement shall remain in force after the termination of said sections.

The "marketing agreement" was a carry-over of the 1933 New Deal program aimed at giving the farmer a parity price, and, to enhance the price of farm produce, authorized production control and marketing agreements. These agreements may fix minimum prices handlers can pay through a control board selected by the Secretary of Agriculture. However, the specific price is not fixed, and the primary aim of the agreement is to control the price by limiting the supply delivered to each market which is done through the control board.

The above three acts constitute the basic legislative exclusion of the agricultural cooperative from the federal anti-trust laws. Concurrently, other legislative favors were being granted. The Stockyard Act of 1921,[17] and the Grain Futures Act of 1922 [18] both specifically limited to agricultural cooperatives an exclusion from the act to such cooperatives' patronage dividends; The Robinson Patman Act,[19] in forbidding price discrimination, provided by Section 4 that the act does not prohibit a cooperative from making a patronage dividend; the Cooperative Marketing Act of 1926 [20] providing for research and advisory services for cooperatives by the Department of Agriculture; there are also favorable

[16] 7 USC Sec. 601 *et seq.*
[17] 7 USC Sec. 181 *et seq.*
[18] 42 Stat. L. 998.
[19] 49 Stat. L. 1526, 15 USC Sec. 13 *et seq.*
[20] 12 Stat. L. 998, 1001.

provisions in others such as the Bituminous Coal Act, Rural Electrification Act, etc.

That Congress has approved the cooperative form of business organization is manifest from the above. First reading of the above statutes would indicate that Congress intended to vest in the Secretary of Agriculture the exclusive power to enforce the federal anti-trust laws as to agricultural cooperatives, and to exclude such cooperatives from the operation of the Sherman Anti-Trust Law. Before making too hasty a determination of the effect of these statutes, one should examine the judicial construction they have received.

That Section 6 of the Clayton Act did not exclude farm cooperatives from the Sherman Act was shown by the case of *United States v. King*.[21] The Aroostook Potato Shippers' Association, a group of dealers in potatoes, blacklisted certain customers whom they, for various reasons, considered undesirable, and circulated the list among members and non-members of the association. The court held that a cooperative is not allowed to adopt a secondary boycott or other measures which are monopolistic in violation of the Sherman Act, and Sec. 6 of the Clayton Act is no protection from a prosecution of such violation.

This case limits the Clayton Act to recognition of the cooperative form as a legal business entity, and not illegal *per se* as they seemingly could be held under the Sherman Act.

The position of the agricultural cooperative under the federal anti-trust laws after enactment of the Capper-Volstead Act and the Agricultural Marketing Agreements Act is well illustrated by the *Borden* case.[22] The five defendants were the milk distributor, a cooperative milk production association, the Milk Wagon drivers' union, municipal officers, and arbitrators of the dispute between the producers and distributors. All were indicted under the Sherman Act for engaging in a combination and conspiracy to restrain trade and commerce in fluid milk among several states by fixing and maintaining prices paid to the producer and charged to consumers, and controlling the supply of milk. The District Court dismissed the indictment stating that the Capper-Volstead Act gave the producers authority to organize and fix and control prices in marketing, and that only the Secretary of Agriculture had the power to intervene, and he only when the price was unduly enhanced by such practices, and further that the Agricultural Marketing Agreement Act removed Farm Cooperatives entirely from the Sherman Act. The United States Supreme Court reversed the District Court, holding that these statutes have not superseded the restrictions of the Sherman Anti-Trust Act so far as cooperatives are concerned. The Capper-Volstead Act authorizes cooperatives to market collectively, but does not authorize cooperatives to conspire with others—cooperative, corporation or individual,

[21] 250 F. 908 (Dist. of Mass. (1916)).

[22] United States v. Borden Co., 308 U. S. 188, 60 S. Ct. 182 (1939).

to fix prices when such a conspiracy violates the Sherman Act. As to the Agricultural Marketing Agreement Act, the court pointed out that the Secretary must act strictly within the procedure set out, and when he so acts and an agreement is entered into, the Sherman Act is not violated even though the cooperative is given a monopoly position; but until there is such action by the Sectary of Agriculture, the cooperative is subject to the Sherman Act.

This and the statement of the Court in *U. S. v. Maryland and Virginia Milk Producers Association*:[23]

> A combination of producers and distributors to eliminate competition and fix prices at successive stages of marketing of an agricultural product is not privileged under the Capper-Volstead or Clayton Acts.

And a similar holding in the *Columbia River Packers Association v. Hinton*,[24] where the cooperative "labor union" of 90% of the troll fishermen in the Washington and Oregon area sought to require purchasers to enter into an exclusive buying contract under the protection of the Fishermen's Collective Marketing Act, which Act was patterned after the Capper-Volstead Act, were held to be in violation of the Sherman Act, seem to justify the remark by Kaminsky:[25]

> It thus appears that what at first seemed unlimited legislative sanction of cooperative activity has been narrowly limited by judicial construction. The extra-judicial powers conferred upon administrative officers must be exercised in the prescribed manner. In the absence of such official participation, cooperatives, in their marketing practices, are still subject to the anti-trust laws.

This appraisal of the situation has certainly not escaped the keen eye of the leaders of the Farm Bloc, as stated by Professor Mund:[26]

> The very fact of their concerted action has given such groups a considerable measure of political unity and has enabled a number of them by means of unified pressure to secure an exemption from the anti-trust laws. For a variety of reasons, however, Congress has been repeatedly induced and persuaded to narrow the field covered by the anti-trust laws and to take long steps toward the acceptance of a system of legalized private monopoly.

That such favors have been obtained from Congress in the past by the Farm Bloc should prove to the most skeptical that,

[23] 179 F. 2d (1949).
[24] 315 U.S. 143, 62 S. Ct. 520 (1942).
[25] 29 Cornell Law Quarterly 251, 256.
[26] Note 1 *supra*, at p. 215.

following setbacks at the hands of the judiciary, additional remedial legislation will be sought and obtained, as well as a continuing program of "educating the Supreme Court".

The foregoing briefly outlines the situation of the agricultural cooperative at the present time in relation to the anti-trust laws. It would appear that we can expect continuing pressure tactics to be applied by the powerful Farm Bloc in Congress for favorable legislation, and from past experience, it would appear that such legislation will be forthcoming, the exact pattern, of course, is impossible to foresee. That the Court is amenable to legislative mandates is clearly indicated by Mr. Justice Black's statement in the *Associated Press* Case:[27]

> It is significant that when Congress has desired to permit cooperatives to interfere with the competitive system of business, it has expressly done so by legislation.

No individual would be so naive as to assert that the average individual farmer has any interest in obtaining a monopolistic position, or has any interest in cooperative action other than achieving a better economic position, that is, higher prices for what he produces and lower prices on the items he must purchase. Neither should any individual be so naive as to believe that the leaders of the cooperative movement and of the Farm Bloc, just as to the leaders of any so-called "Big Business", would not use monopolistic practices to achieve those ends. Improvement of the economic situation of the farmer is highly desirable, but a monopolistic control over the marketing of farm produce through closely integrated agricultural cooperatives is as highly undesirable. The ultimate conflict, economically speaking, is between the consumer and the producer, and greatly overshadows the present labor-management dispute. Continued growth of the cooperative movement under a favored legal position could very easily swing the pendulum in favor of the agricultural producer, just as we have seen an extreme in labor-management relations under pro-labor legislation. Therefore, future legislative as well as judicial trends should be watched with interest, as well as alarm.

It is submitted that legislative action to prevent agricultural cooperatives obtaining monopolistic control of production of a particular product should be directed at the following: (1) limitations on the right of cooperatives to federate to form common marketing agencies; (2) prohibition of the establishment by cooperatives of production control on members; (3) limitation on the size of cooperatives, either by area or percentage of total production. It is felt that such legislation would preserve the advantages of cooperation without sacrificing our basic economic policy, a competitive market.

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[27] 326 U.S. 1, 65 S. Ct. 1416 (1945).