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on

## "OPEN PRICE ASSOCIATIONS"

by

Huston Thompson, Commissioner, Federal Trade Commission.

### I N T R O D U C T I O N

It is a great pleasure to renew associations with your organization after a most pleasant time with you last year at Cleveland. I find myself sandwiched in a most sympathetic company.

Your first speaker, the eminent Secretary of Agriculture, for years has been a staunch supporter of progressive ideals in government. Since he has come into official life, there has been transferred to his department the supervision of the meat packing industry, an industry which you are all aware the Federal Trade Commission investigated for some years. It is a great pleasure to state at this time that information has come to me that Mr. Wallace is handling this most difficult task in an admirable way. You also have selected as your final speaker tonight, Senator Capper of Kansas, who in a very short time became one of the leaders of the United States Senate and of the whole nation.

It may only be a coincident, but nevertheless an interesting one, that all of the speakers of the evening together with the lady who is presiding come from west of the Mississippi River, beginning with Iowa, then Kansas and finally Colorado.

We are all from the region of the open country and it may be that had something to do with your Chairman tagging me with the subject of open price associations for discussion this evening.

I come neither to praise or condemn the subject assigned to me, nor to indulge in any personalities, a thing which I think is usually futile. I shall try to take the subject and turn it inside out, and let you see it as one who has been down into the very vitals of this question. I shall abstain as far as possible from voicing any subjective opinions and shall paint the picture to you in quotations from letters of those in the industries and from historical facts which have come to my observation.

Now the most interesting thing about the work of the Federal Trade Commission is that when an economic situation is presented for the first time to us, and we think that we have hold of something new owing to the fact that life has changed, invariably we find, if we search back in history, a prototype, and in the case of "open price associations", there is no exception to the rule.

### THE GUILDS OF THE MIDDLE AGES

Back in the Middle Ages, after the nations had changed from the nomadic life to the agrarian, and drifted from the agrarian into a situation where people congested into cities, so that urban or community life dominated, there developed what are known as guilds.

These guilds centered around communities. They started off with high and praiseworthy ideals, namely the advancement of trade in their particular communities. They had not gone very far, however, until they began to split up

into numerous guilds and a situation arose not unlike that described by Carlyle in his "French Revolution", where, speaking of the situation into which the French Government had gotten itself in the survey of private business, it had become necessary not only to have an inspector of pigs, but also an inspector of suckling pigs.

While the guilds had many admirable points about them, they drifted into policies where one of the dominating purposes was the maintaining of prices and the curtailment of production, which resulted in choking the channels of trade and making the guilds so obnoxious that finally the people of England with far-sighted wisdom cut the Gordian knot. Thoroughgoing reforms were made involving particularly the elimination of the unfair trade practices and monopolistic activities that had grafted themselves on to the guilds like barnacles on a ship. England saved herself thereby from a revolution.

France, on the other hand, failed to eliminate these evils, until the oppression became so great and produced such a narrowing and suppressing effect on the middle class and the peasantry that this factor, together with the oppression exercised by the aristocracy, brought on the French Revolution.

#### WHAT IS MEANT BY OPEN PRICE ASSOCIATION?

Now, keeping in mind the fact that the guilds were associations which permitted the barnacles of destruction to be grafted onto them, let us first of all find out what we mean by "open price associations", and at this point clearly distinguish between the "open price association" and the ordinary trade association. Trade association is the broader term, and an "open price association", is but one form of trade association.

Trade associations, speaking generally, have undoubtedly done a great deal of good for their particular industries, and I can say, positively, that in dealing with trade associations which were not open price associations, the Federal Trade Commission has frequently had splendid assistance and cooperation, and the results obtained were very much worth while.

If I were to talk on the broad subject of trade associations tonight, I could easily discuss for hours how many of them have come voluntarily to the Commission and with a fine spirit sought to eliminate the wrong practices within their own organizations, and have given support to their secretaries, even to the point of having the secretaries give the information on which complaints were filed before the Commission, against individual members, something which I think you will agree with me testifies to an admirable and public spirited sense of duty.

It should be perfectly clear, therefore, that we are not now discussing trade associations generally but are limiting ourselves to "open price associations".

Now what is an "open price association"? I presume the best way to reach a clear understanding is to define that term.

It is an association based upon the proposition that "knowledge regarding prices actually made is all that is necessary to keep prices at reasonably stable and normal levels", and for this purpose the members are to exchange currently and constantly, through central headquarters, "information as to orders, production and shipments." This information is immediately tabulated, and at the very earliest moment, is passed back to all the members.

CAN HUMAN BEINGS EXCHANGE INFORMATION REQUIRED BY OPEN  
PRICE ASSOCIATIONS AND AVOID CURTAILING PRODUCTION,  
THAT RESULTS IN EITHER PRICE FIXING, OR PRICE INCREASE?

The "open price association" is connected with the name of its chief proponent, a man by the name of Eddy, who wrote a book called "The New Competition". Undoubtedly Mr. Eddy believed what he wrote. Perhaps being a lawyer, he could sit in his office and take the abstract plan of an open price association and gazing at its cold type and excluding the human equation believe that such a practice could be put into action without fixing prices, or enhancing prices through concerted curtailment of production at which time the public invariably buys hysterically.

I say Mr. Eddy may have been able to conceive this owing to the fact that he was a lawyer and accustomed to study things in the cold abstract. But the reports of the Federal Trade Commission on a number of large industrial organizations, have shown this theory to be wrong. One industry, for instance, is found to be divided up into ten great regional organizations and those organizations subdivided into many minor organizations according to some 25,000 letters passing between its members. It is clear that prices were fixed or that a curtailment of production was effected which produced a panic buying market resulting in the price of its product jumping approximately 300% and up to the point where the ultimate consumer either could not or would not buy. I may say that of the open price associations that I have investigated, I have never found one that did not either fix prices or cause curtailment of production to the point where it ultimately paralyzed the market.

The Lockwood Investigation, together with investigations recently made in other parts of the country, would seem to indicate beyond peradventure that the actions of these open price associations do result in price fixing or price enhancement.

#### THE EXTENT OF OPEN PRICE ASSOCIATIONS.

A great deal has been said recently about the extent of open price associations, and emphasis given to the effect that there were not very many of them. I am not prepared to say how many there are.

The commission sent out questionnaires to several thousand trade associations in this country. Replies were received from 1515, or about 55% of the organizations addressed. From these, the following information was received. There were 150 associations which distributed or exchanged price information; 324 associations compiled and distributed other trade statistics, not including prices; 799 were non-statistical associations, while 150 associations were inactive or disbanded. Incomplete replies were received from 92 associations. Most of the 150 open price associations also distributed or exchanged information on other features of business, such as orders received, purchases, production, stocks, costs of production and merchandising and matters of general interest to the members.

About 1,000 did not reply to the questionnaires, so we do not know about them, while many others had gone out of existence, and still others would not admit that they were fixing prices, but did admit meeting and exchanging certain statistics. The emphasis, however, should not be laid upon the number of open price associations but rather upon their size and also upon the number and size of the corporations which are members of such associations.

The tobacco investigation of the commission reveals the fact that in practically every field of the industry in which the Commission made an investigation, there were price fixing associations. Likewise in lumber, the United States is divided up into districts according to the type of lumber found.

the largest one of the regional lumber associations 60 percent of the production of the industry was represented by open price organizations.

One association represented 80 percent of the lumber manufacturers of Idaho, Western Montana and Eastern Washington and Eastern Oregon.

The Lockwood investigation likewise reveals open price associations of tremendous proportions.

#### DO OPEN PRICE ASSOCIATIONS STABILIZE BUSINESS?

The great argument made by those in favor of open price associations is that they stabilize business. We have just come through one of the greatest periods of inflation ever known, having reached a climax where the public ceased buying. We have been for sometime in a period of stagnation from which we are all hoping to emerge at an early date. During all of this period open price associations have been more or less in existence. At least, a great number of them were in existence from the time when prices started to climb until the recent decisions of the Supreme Court of the United States, in the American Column and Lumber Company case.

Did the open price associations help to stabilize business during this chaotic period? The answer is known to all of us.

Is it not a fact that the reports of the Federal Trade Commission show that these organizations not only did not attempt to hold back their individual members from advancing prices, but the one deep, dominant note of the whole movement was an increase in prices.

Out of such experiences are we able to say that such organizations, from an economic point of view, have justified their existence? And so long as those who control them are human beings, is it possible to avoid the fixing of prices and tendency to curtailment of production?

#### ARE THE BUSINESS MEN IN DOUBT?

Some business men say they do not know how far they can go within the law. Perhaps the trouble is in dwelling too much on the idea of how far.

Let us take a few of the practices that have been revealed by the Lockwood investigation, the Federal Trade Commission investigations and recent cases that have been before our courts, and see if business men need to be instructed in regard to them.

In the tobacco report, mentioned above, the jobbers and manufacturers were charged with intimidating those who cut prices below the prices fixed by the price-fixing associations, and this was done in spite of the fact that those who sold below the prices fixed by the associations made profits. Does a business man need to be told that he can not conspire with others to intimidate those who do not wish to follow these price-fixing schemes? Or, to look at it from another angle, is the question of doubt one that hangs on the right to blacklist those who will not follow the dictates of a group in business, where the one blacklisted is showing great normal courage, is seeking to act for the good of the public at large, and is not ruining himself, a situation which occurs in every industry?

Perhaps the puzzled inquirer has been in doubt as to whether he could force those to whom he sold his products to maintain prices fixed by him, and for the purpose of carrying out his plan induced those to whom he sold not to

sell to others who did not maintain such prices, and required all those to whom he sold, to report the names of those not keeping the resale price. His doubts should be entirely swept away by the recent decision of the Supreme Court in the Beechnut case.

Does he argue that he does not know whether he can tie a purchaser to himself by contract so that that purchaser can not use the goods of any other person? If so, he has had his pathway lighted by the very recent decision of the Supreme Court in the Standard Fashion Company v. Magrane-Houston Company.

Perhaps he has been seeking, where he owned a patent, to compel others not to use in connection with the patented article any goods except those sold by the owner of the patent. Here again the driftwood is cleared away, for there is a bright light of a very recent supreme court decision to guide his wandering footsteps.

Is it simulation of a competitor's name on goods? Or fraudulent advertising, or commercial bribery? Can it be a plan where in an open price association, the competitors come together and interchange reports as to orders, production, shipments, etc?

Listen to what the Supreme Court of the United States says about such a plan: "Such close cooperation between many persons, firms, and corporations, controlling a large volume of interstate commerce as is provided for in this 'plan', is plainly, in theory as it proved to be in fact, inconsistent with that free and unrestricted trade which the statute contemplates should be maintained \* \* \* \*".

What is it then that confuses some of the businessmen? I say some because there are many men in the business world whom I have had the pleasure of conferring with, who have no more doubts about what these practices mean than has the Supreme Court of the United States. Mr. Taft, the present Chief Justice of that Court, as far back as 1911, in answer to a similar statement to the effect that business was groping in the dark, confidently asserted that: "The business community now knows or ought to know where it stands".

Will such gentlemen who are in the fog please tell us just what it is that makes the fog, or what it is that confuses them?

#### HOW DOES THE OPEN PRICE ASSOCIATION FUNCTION IN REALITY AND DOES IT AFFECT THE PUBLIC AT LARGE?

In response to a Senate Resolution, the Commission investigated the subject of the price of tobacco products. The report which the commission made reveals the domestic situation with respect to the farmers who are the producers, the jobbers and the manufacturers of this product. In substance, this report shows that the jobbers of this country associated together in open price associations which resulted in price-fixing; that they called upon the manufacturers, and with one notable exception, worked together with the manufacturers to keep up prices so that at the date of the Commission's report, the prices charged by the manufacturer for tobacco products have remained practically constant at the high levels obtaining in 1919. The Commission said that this was due in part at least to "the jobbers' price-fixing agreements."

On the other hand, while no conclusive evidence was found of collusion to depress prices paid to the grower for tobacco, it "appears that a few large buyers had a dominant position and each purchased only a certain percentage of the offerings; that common buying agencies were used, and that secret purchases were made through independent dealers while the ultimate purchasers held off the market, or practically so".

Here we have a most revealing picture. The jobbers and the manufacturers are holding up the prices, while, at the same time, the manufacturers practically stay off the market to such an extent that prices dropped to a point where the farmer was helpless. In other words, the phrase which we find in Mr. Eddy's book as well as in the letters of those carrying on open price associations to the effect that they must not kill the goose that laid the golden egg, figuratively speaking, made a fact. This picture of conditions in the tobacco world is a cross section of what has been going on in the rest of the business world, and as a result the purchasing public has become prostrated.

Thirty years ago, seventy per cent. of our people lived or worked on farms. Today 48% are on farms, despite the fact that our Secretary of Agriculture, and his predecessors have been doing everything possible in their line to assist the farmer.

Is it not time that we should open up the channels of trade so that the cycle from producer to consumer and back again should be unfettered? And the producer, who in this case is also the ultimate consumer, should be left with at least the wherewithal to purchase that which the manufacturers and distributors have for sale?

What has been the reaction in the tobacco world? Today two tremendous cooperative organizations of farmers have formed to meet the situation which has been brought on by the jobbers and manufacturers.

While many open priced organizations undoubtedly started out with the best of purposes, just as the guilds did and in bold declarations in their minutes and by-laws, declared against price fixing, it is interesting to trace their steps and see where, under this open price association plan, human nature finally gets the upper hand.

We have an association marketing oil in one of our Western cities. This association covers a very large area in which live many people. Each year the city referred to asks for bids on the oil and gasoline which was necessary for its public utilities. Now a strange thing happened. Only four of the members of this association handed in bids and when the bids are opened, they were found to be identical.

The minutes of the association contained no evidence of collusion, or price fixing, or anything of that sort. And when the Secretary of this organization, of his own volition came before the Commission, he insisted that nothing has been done in the meetings with regard to price fixing. Whereupon the following questions were put by the Commissioners or their representative.

Q. Was it agreed at the meeting that only the four companies should bid?

A. No.

Q. Why wasn't it entered? What was the reason for the preparation and issuance of the memoranda at these various meetings that don't appear in the record of the meetings?

A. Because they were not a part of the business of the meeting. These conferences, or whatever they may be, mostly occurred out in the hall after the meeting, or at other offices.

Q. Among the members of the Association?

A. Yes.

Q. That is interesting. These memoranda are quite apart from the regular minutes?

A. Yes.

Q. Now, Mr. Secretary, we have had had similar cases. You have been secretary for a long while; how is that done? You hold a meeting; it must be called to order and certain things done, all of which are mentioned. Then do they drift out and hold another meeting? I would like to know.

A. They go out arm in arm. The chances are they haven't seen each other for a week. After the crowd is outside they do the real thing they are interested in.

Q. How do they get it to you? Are you part of the crowd as it drifts out?

A. Frequently a part of the crowd. \* \* \* \* "

In the lumber industry the cold abstract open price association device becomes tangled up with human nature in a most remarkable way.

The operations of the largest association in the industry centered around the use of a device known as a trade barometer, by which, through concerted action, the Association instructs its membership how to restrict production and thereby to increase the price of lumber, by an artificial control of supply as balanced against current demand.

This barometer was issued to the members of the Association weekly. It is portrayed on the right hand side of a sheet of paper and consists of a bulb out of which arise three perpendicular tubes. The first tube is designated by the word "orders", the second by the word "production", and the third by the word "shipments".

In order to make the information portrayed by the barometer striking to the eye, red colors are used in the bulb and tubes.

Whenever the members see that the red in the middle tube entitled "production" stands higher than the red in the first and third tubes known as "orders" and "shipments", they see at once that production must be decreased on the theory that if it is not, there will be an over supply in the market which will force down prices.

If, however, the barometer shows that the red of the middle tube, indicating production, is below the red in the other two tubes, indicating orders and shipments, then the members see that supply is below demand and that higher prices can be obtained.

This device for restricting production was inaugurated in 1915. At that time there was printed on the upper left hand corner of the barometer and just outside of the "order" tube the words "Marketing Advancing". Directly opposite in the upper right hand corner and just outside the "shipment" tube appeared the words "Increase Production". On the lower left hand corner were the words "Market Declining", and just opposite, on the lower right hand corner the words "Decrease Production."

Thus the height of the red color in the respective tubes automatically indicated which of these instructions were to be applied.

The theory of the device was described by the President of the Association, in a letter as follows:

The Association will shortly get out a weekly barometer, which has been submitted to our counsel and which meets with their approval. This barometer will automatically forecast market conditions, and it is based on orders received and shipments made. Where the shipments exceed the

orders, it indicates an advancing market, and whenever the reverse is true it indicates a falling market. Then once a month we will get out another barometer based on the production, which will indicate an advancing market when shipments are in excess of production, and a falling market when the reverse is true, advising increase of production when the orders and shipments are in advance of production and a decrease in production when the production is in excess of orders and shipments. This will give the information graphically.

Shortly after the barometer was circulated among the Association members, the President of a certain company, wrote to the President, and to Secretary and Manager of his association, advising that the words "increase production", be taken off, stating that "this is just the condition that we wish to avoid." Following this he said, "is it not possible that some of our members might construe your weekly letter, bearing this label, as advice from our Association, to cut loose and resume night sawing with their mills?" and again, "Some cautionary advice should be inserted, bringing home to our members the truth of the old adage, 'Do not kill the goose that lays the golden eggs.'"

The writer's advice was followed and the four phrases, "market advancing", "increase production", and "market declining", "decrease production," were removed. The following statement from another letter is illuminating:

"In preparing the barometer, the attorneys thought that if we were going to show 'decrease production' thereon, 'increase production' ought to go on too; So while we are not advising our people what to do, the barometer itself will tell the story."

It should be stated that while these four phrases were removed, there still remained beneath the barometer the following language:

#### "TRADE BAROMETER"

"Whenever Shipments or Orders are below Production, experience indicates an over-production, with consequent lowering values.

"Experience indicates that whenever Shipments or Orders are above Production, values increase, provided Production does not increase at a greater ratio than Shipments and Orders."

The foregoing quotation appeared beneath the barometer continuously until October, 1919.

It should be noted in respect to the date, October, 1919, that at this time the Commission was preparing to make an investigation of the lumber industry as requested by the Department of Justice but had not yet actually begun. However, the fact of this request had been ascertained and had been spread through the industry. Shortly after this, the language just quoted was removed.

In addition to the barometer, meetings of the different groups of employees such as the salesmen, were held from time to time. There was constant urging in specific language toward curtailment of production and increase in prices, until the country became hysterical in its buying and the price of lumber, for example, in one district jumped from \$13.40 in 1915 to \$55.55 a thousand in 1920, with a margin of profit in 1915 of \$1.09 a thousand to \$26.35 a thousand in 1920, and this despite the fact that in this industry its protests were made against these advances by men patriotic and loyal within the association itself who were swept along in the tide of the so-called stabilizing movement.



## CONCLUSION

Is it not well to ask ourselves whether we can afford to permit the practices of open price associations and whether they shall lead us to the situations that the guilds brought upon the whole world in days past?

After all is there any way out of the present economic situation except by keeping clear the channels of trade and keeping alive the competitive system?

All nations have started off in their virile youth with competition and continued to follow this policy until they waxed fat and ceased to preserve the individual initiative and personality. When that stage was reached, they have invariably grafted upon themselves the insidious tendencies toward monopoly and have then gone down.

You women are the keepers of the household. As you know, the word "economist" interpreted from the Greek means the keeper of the household, and as one who watches over its purchases. It devolves upon you principally to keep the family as the unit in America and to preserve in all its integrity our noble youth and in doing this it becomes your duty to see to it that the competitive system is kept alive.

You have come into the political world at a time when the whole economic system is calling for clear thinking and high purpose. If you will resolve all of these questions, such as the open price association in the light of what is best for the American home, you will reach a conclusion both on the economic and legal phase of the questions before this country which will mean safety and perpetuity not only for our government, but for the family life of this nation.

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