NOTE

In June 1933, FDR signed into law the National Industrial Recovery Act that partially suspended antitrust law and created a regulatory framework for the facilitation and enforcement of industry collaborations. The Supreme Court handed down *Appalachian Coals* three months earlier.

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Appalachian Coals v. United States

288 U.S. 344 (March 13, 1933)

Mr. Chief Justice HUGHES delivered the opinion of the Court.

This suit was brought to enjoin a combination alleged to be in restraint of interstate commerce in bituminous coal and in attempted monopolization of part of that commerce, in violation of sections 1 and 2 of the Sherman Anti-Trust Act. . . .

Defendants, other than Appalachian Coals, Inc., are 137 producers of bituminous coal in eight districts (called for convenience Appalachian territory) lying in Virginia, West Virginia, Kentucky, and Tennessee. . . . In 1929 (the last year for which complete statistics were available) the total production of bituminous coal east of the Mississippi river was 484,786,000 tons, of which defendants mined 58,011,367 tons, or 11.96%. In the so-called Appalachian territory and the immediately surrounding area, the total production was 107,008,209 tons, of which defendants' production was 54.21%, or 64% if the output of 'captive' mines (16,455,001 tons) be deducted.[1] With a further deduction of 12,000,000 tons of coal produced in the immediately surrounding territory, . . . defendants' production in the latter region was found to amount to 74.4%.

The challenged combination lies in the creation by the defendant producers of an exclusive selling agency, [Appalachian Coals, Inc]. Defendant producers own all its capital stock, their holdings being in proportion to their production. The majority of the common stock, which has exclusive voting right, is held by seventeen defendants. [The company has an exclusive right to sell] all coal (with certain exceptions) [produced by the defendants]. The Company agrees to establish standard classifications, to sell all the coal of all its principals at the best prices obtainable and, if all cannot be sold, to apportion orders upon a stated basis. The plan contemplates that prices are to be fixed by the officers of the Company at its central office. . . . The Company is to be paid a commission of 10% of the gross [sales]. . . .

The Government's contention, which the District Court sustained, is that the plan violates the Sherman Anti-Trust Act [because] it eliminates competition among the defendants themselves and also gives the selling agency power substantially to affect and control the price of bituminous coal in many interstate markets. [The district court found] that this elimination of competition and concerted action will affect market conditions, and have a tendency to stabilize prices and to raise prices to a higher level than would prevail under conditions of free competition. The court added that the selling agency will not have monopoly control of any market nor the power to fix monopoly prices.

[1] 'Captive' mines are thus designated as they produce chiefly for the consumption of the owners.

Defendants insist that the primary purpose of the formation of the selling agency was to increase the sale, and thus the production . . . through better methods of distribution, intensive advertising and research, to achieve economies in marketing, and to eliminate abnormal, deceptive, and destructive trade practices. They disclaim any intent to restrain or monopolize interstate commerce. [The evidence shows that defendants] have been acting fairly and openly, in an attempt to organize the coal industry and to relieve the deplorable conditions resulting from overexpansion, destructive competition, wasteful trade practices, and the inroads of competing industries. . . .

First. There is no question as to the test to be applied in determining the legality of the defendants' conduct. The purpose of the Sherman Anti-Trust Act is to prevent undue restraints of interstate commerce, to maintain its appropriate freedom in the public interest, to afford protection from the subversive or coercive influences of monopolistic endeavor. As a charter of freedom, the act has a generality and adaptability comparable to that found to be desirable in constitutional provisions. It does not go into detailed definitions which might either work injury to legitimate enterprise or through particularization defeat its purposes by providing loopholes for escape. The restrictions the act imposes are not mechanical or artificial. Its general phrases, interpreted to attain its fundamental objects, set up the essential standard of reasonableness. They call for vigilance in the detection and frustration of all efforts unduly to restrain the free course of interstate commerce, but they do not seek to establish a mere delusive liberty either by making impossible the normal and fair expansion of that commerce or the adoption of reasonable measures to protect it from injurious and destructive practices and to promote competition upon a sound basis. . . .

In applying this test, a close and objective scrutiny of particular conditions and purposes is necessary in each case. Realities must dominate the judgment. The mere fact that the parties to an agreement eliminate competition between themselves is not enough to condemn it. . . . The familiar illustrations of partnerships, and enterprises fairly integrated in the interest of the promotion of commerce, at once occur. The question of the application of the statute is one of intent and effect, and is not to be determined by arbitrary assumptions. It is therefore necessary in this instance to consider the economic conditions peculiar to the coal industry, the practices which have obtained, the nature of defendant's plan of making sales, the reasons which led to its adoption, and the probable consequences of the carrying out of that plan in relation to market prices and other matters affecting the public interest in interstate commerce in bituminous coal.

Second. The findings of the District Court, upon abundant evidence, leave no room for doubt as to the economic condition of the coal industry. That condition, as the District Court states, 'for many years has been indeed deplorable.' Due largely to the expansion under the stimulus of the Great War, 'the bituminous mines of the country have a developed capacity exceeding 700,000,000 tons' to meet a demand 'of less than 500,000,000 tons.' In connection with this increase in surplus production, the consumption of coal in all the industries which are its largest users has shown a substantial relative decline. The actual decrease is partly due to the industrial condition but the relative decrease is progressing, due entirely to other causes. Coal has been losing markets to oil, natural gas and water power and has also been losing ground due to greater efficiency in the use of coal. The change has been more rapid during the last few years by reason of the developments of both oil and gas fields. . . . [T]he adverse influence upon the coal industry, including the branch of it under review, of the use of substitute fuels and of improved methods is apparent. . . .

This unfavorable condition has been aggravated by particular practices [that the Court described as "destructive"]. . . . 'Pyramiding' of coal is [an example of a] 'destructive practice.' It occurs when a producer authorizes several persons to sell the same coal, and they may in turn offer it for sale to other dealers. In consequence 'the coal competes with itself, thereby resulting in abnormal and

destructive competition which depresses the price for all coals in the market.' Again, there is misrepresentation by some producers in selling one size of coal and shipping another size which they happen to have on hand. . . . [Such practices] have been injurious to the coal industry as a whole. [However, there was no evidence showing] the existence of any trade war or widespread fraudulent conduct. The industry also suffers through 'credit losses,' which are due to the lack of agencies for the collection of comprehensive data with respect to the credits that can safely be extended.

[Additionally,] organized buying agencies, and large consumers purchasing substantial tonnages, 'constitute unfavorable forces. The highly organized and concentrated buying power which they control and the great abundance of coal available have contributed to make the market for coal a buyers' market for many years past.

It also appears that the 'unprofitable condition' of the industry has existed particularly in the Appalachian territory where there is little local consumption as the region is not industrialized. The great bulk of the coal there produced is sold in [highly competitive regions]. . . . [N]umerous producing companies have gone into bankruptcy or into the hands of receivers, many mines have been shut down, the number of days of operation per week have been greatly curtailed, wages to labor have been substantially lessened, and the states in which coal producing companies are located have found it increasingly difficult to collect taxes.

Third. The findings also fully disclose the proceedings of the defendants in formulating their plan and the reasons for its adoption. The serious economic conditions had led to discussions among coal operators and state and national officials, seeking improvement of the industry. . . . [These meetings] resulted in the organization of defendant Appalachian Coals, Inc. It was agreed that a minimum of 70% and a maximum of 80% of the commercial tonnage of the territory should be secured before the plan should become effective. Approximately 73% was obtained. A resolution to fix the maximum at 90% was defeated. The maximum of 80% was adopted because a majority of the producers felt that an organization with a greater degree of control might unduly restrict competition in local markets. The minimum of 70% was fixed because it was agreed that the organization would not be effective without this degree of control. The court below also found that it was the expectation that similar agencies would be organized in other producing districts including those which were competitive with Appalachian coal, and that it was 'the particular purpose of the defendants in the Appalachian territory to secure such degree of control therein as would eliminate competition among the 73% of the commercial production.' . . .

When, in January, 1932, the Department of Justice announced its adverse opinion, the producers outside Appalachian territory decided to hold their plans in abeyance pending the determination of the question by the courts. . . .

Defendants refer to the statement of purposes in their published plan of organization—that it was intended to bring about 'a better and more orderly marketing of the coals from the region to be served by this company (the selling agency) and better to enable the producers in this region, through the larger and more economic facilities of such selling agency, more equally to compete in the general markets for a fair share of the available coal business.' The District Court found that among their purposes, defendants sought to remedy 'the destructive practice of shipping coal on consignment without prior orders for the sale thereof, which results in the dumping of coal on the market irrespective of the demand'; 'to eliminate the pyramiding of offers for the sale of coal'; to promote 'the systematic study of the marketing and distribution of coal, the demand the the consumption and the kinds and grades of coal made and available for shipment by each producer in order to improve conditions'; to maintain an inspection and engineering department which would keep in constant

contact with customers 'in order to demonstrate the advantages and suitability of Appalachian coal in comparison with other competitive coals'; to promote an extensive advertising *367 campaign which would show 'the advantages of using coal as a fuel and the advantages of Appalachian coal particularly'; to provide a research department employing combustion engineers which would demonstrate 'proper and efficient methods of burning coal in factories and in homes' and thus aid producers in their competition with substitute fuels; and to operate a credit department which would build up a record with respect to the 'reliability of purchasers.' The court also found that 'defendants believe that the result of all these activities would be the more economical sale of coal, and the economies would be more fully realized as the organization of the selling agent is perfected and developed.' But in view of the designation of subagents, economies in selling expenses would be attained 'only after a year or so of operation.'

No attempt was made to limit production. The producers decided that it could not legally be limited and, in any event, it could not be limited practically. The finding is that 'it was designed that the producer should produce and the selling agent should sell as much coal as possible.' The importance of increasing sales is said to lie in the fact that the cost of production is directly related to the actual running time of the mines.

Fourth. Voluminous evidence was received with respect to the effect of defendants' plan upon market prices. As the plan has not gone into operation, there are no actual results upon which to base conclusions. The question is necessarily one of prediction. The court below found that, as between defendants themselves, competition would be eliminated. This was deemed to be the necessary consequence of a common selling agency with power to fix the prices at which it would make sales for its principals. Defendants insist that the finding is too broad. . . .

The more serious question relates to the effect of the plan upon competition between defendants and other producers. As already noted, . . . the great bulk of the coal produced in Appalachian territory is sold in [highly competitive regions]. . . . [The evidence] fails to disclose an adequate basis for the conclusion that the operation of the defendants' plan would produce an injurious effect upon competitive conditions. . . . While strikes and interruptions of transportation may create temporary and abnormal dislocations, the bituminous coal industry under normal conditions affords most exceptional competitive opportunities. . . . Conditions in the coal industry are such that new companies are free to enter the business of producing and marketing coal in competition with existing companies. [Additionally], the 'highly organized and concentrated buying power' that can be exerted must [receive] appropriate consideration.

Consumers testified that defendants' plan will be a benefit to the coal industry and will not restrain competition. . . . Competing producers testified that the operation of the selling agency, as proposed by defendants, would not restrain competition and would not hurt their business. . . .

Fifth. We think that the evidence requires the following conclusions:

1. With respect to defendant's purposes, we find no warrant for determining that they were other than those they declared. Good intentions will not save a plan otherwise objectionable, but knowledge of actual intent is an aid in the interpretation of facts and prediction of consequences. . . . The evidence leaves no doubt of the existence of the evils at which defendants' plan was aimed. The industry was in distress. It suffered from overexpansion and from a serious relative decline through the growing use of substitute fuels. It was afflicted by injurious practices within itself—practices which demanded correction. If evil conditions could not be entirely cured, they at least might be alleviated. The unfortunate state of the industry would not justify any attempt unduly to restrain competition or to monopolize, but the existing situation prompted defendants to make, and the statute did not

preclude them from making, an honest effort to remove abuses, to make competition fairer, and thus to promote the essential interests of commerce. The interests of producers and consumers are interlinked. When industry is grievously hurt, when producing concerns fail, when unemployment mounts and communities dependent upon profitable production are prostrated, the wells of commerce go dry. So far as actual purposes are concerned, . . . defendants were engaged in a fair and open endeavor to aid the industry in a measurable recovery from its plight. The inquiry then, must be whether despite this objective the inherent nature of their plan was such as to create an undue restraint upon interstate commerce.

2. The question thus presented chiefly concerns the effect upon prices. . . . [T]he conditions of the production and distribution of bituminous coal, the available facilities for its transportation, the extent of developed mining capacity, and the vast potential undeveloped capacity, makes it impossible to conclude that defendants through the operation of their plan will be able to fix the price of coal in the consuming markets. . . . Defendants' coal will continue to be subject to active competition. . . . The plan cannot be said either to contemplate or to involve the fixing of market prices.

The contention is, and the court below found, that while defendants could not fix market prices, the concerted action would 'affect' them, that is, that it would have a tendency to stabilize market prices and to raise them to a higher level than would otherwise obtain. But the facts [do not support the conclusion that this arrangement] will be detrimental to fair competition. A co-operative enterprise, otherwise free from objection, which carries with it no monopolistic menace, is not to be condemned as an undue restraint merely because it may effect a change in market conditions, where the change would be in mitigation of recognized evils and would not impair, but rather foster, fair competitive opportunities.

Voluntary action to rescue and preserve these opportunities, and thus to aid in relieving a depressed industry and in reviving commerce by placing competition upon a sounder basis, may be more efficious than an attempt to provide remedies through legal processes. The fact that the correction of abuses may tend to stabilize a business, or to produce fairer price levels, does not mean that the abuses should go uncorrected or that co-operative endeavor to correct them necessarily constitutes an unreasonable restraint of trade. The intelligent conduct of commerce through the acquisition of full information . . . may properly be sought by the co-operation of those engaged in trade, although stabilization of trade and more reasonable prices may be the result. *Maple Flooring Manufacturers' Association v. United States*, 268 U.S. 563 (1925). Putting an end to injurious practices, and the consequent improvement of the competitive position of a group of producers is not a less worthy aim and may be entirely consonant with the public interest, where the group must still meet effective competition in a fair market and neither seeks nor is able to affect a domination of prices. . . .

3. The question remains whether, despite the foregoing conclusions, the fact that the defendants' plan eliminates competition between themselves is alone sufficient to condemn it. Emphasis is placed upon defendants' control of about 73% of the commercial production in Appalachian territory. But only a small percentage of that production is sold in that territory. . . . Defendants must go elsewhere to dispose of their products. . . . [N]o valid objection could have been interposed under the Sherman Act if the defendants had eliminated competition between themselves by a complete integration of their mining properties in a single ownership. . . . We agree that there is no ground for holding defendants' plan illegal merely because they have not integrated their properties and have chosen to maintain their independent plants, seeking not to limit but rather to facilitate production. We know of no public policy, and none is suggested by the terms of the Sherman Act, that in order to comply with the law those engaged in industry should be driven to unify their properties and businesses in order to correct abuses which may be corrected by less drastic measures.

Public policy might indeed be deemed to point in a different direction. If the mere size of a single, embracing entity is not enough to bring a combination in corporate form within the statutory inhibition, the mere number and extent of the production of those engaged in a co-operative endeavor to remedy evils which may exist in an industry, and to improve competitive conditions, should not be regarded as producing illegality. The argument that integration may be considered a normal expansion of business, while a combination of independent producers in a common selling agency should be treated as abnormal—that one is a legitimate enterprise and the other is not—makes but an artificial distinction. The Anti-Trust Act aims at substance. Nothing in theory or experience indicates that the selection of a common selling agency to represent a number of producers should be deemed to be more abnormal than the formation of a huge corporation bringing various independent units into one ownership. . . . The question in either case is whether there is an unreasonable restraint of trade or an attempt to monopolize. If there is, the combination cannot escape because it has chosen corporate form, and, if there is not, it is not to be condemned because of the absence of corporate integration. As we stated at the outset, the question under the act is not simply whether the parties have restrained competition between themselves but as to the nature and effect of that restraint. . . .

The decree will be reversed, and the cause will be remanded to the District Court with instructions to enter a decree dismissing the bill of complaint without prejudice and with the provision that the court shall retain jurisdiction of the cause any may set aside the decree and take further proceedings if future developments justify that course in the appropriate enforcement of the Anti-Trust Act.

It is so ordered.