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Wallace C. Murchison

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SIGNIFICANCE OF THE AMERICAN TOBACCO COMPANY CASE

WALLACE C. MURCHISON*

Walter Lippmann once defined competition as something of which producers have only as much as they cannot eliminate.\(^1\) Certainly efforts to eliminate competition have been at least as characteristic of the American economy as competition itself. Free enterprise has been under almost continuous attack by entrepreneurs who have attempted to substitute trusts, combinations, price-fixing agreements, patent pools, and so on for the automatic market mechanism under which price equates supply and demand in a competitive system. To all such attempts the Sherman Anti-Trust Act\(^2\) opposes a legal barrier. Its broad prohibitions against restraints of trade and monopolies have been judicially applied to meet each new threat, each new device which business ingenuity has developed. Under it courts have condemned both the crude predatory practices of the early trusts and the more subtle illegalities of trade association statistical services. It is in the adaptability of federal anti-trust enforcement to the changing masquerade of monopoly that its strength and its possibilities for the future lie. Illustrative of this adaptability and suggestive of future action under the Act is the American Tobacco Company case,\(^3\) decided by the Supreme Court, in June, 1946.

THE CASE

The Supreme Court decision was the culmination of six years of complex and costly litigation.\(^4\) On July 24, 1940 a criminal information\(^5\) was filed in the federal court for the Eastern District of Kentucky, charging eight major tobacco companies,\(^6\) their subsidiaries and officials, with violation of Sections 1 and 2\(^7\) of the Sherman Act.\(^8\) The informa-

* Member of the Wilmington North Carolina Bar.
\(^1\) Quoted in *Hearings before the Temporary National Economic Committee, Part 25, 76th Cong., 3d Sess. 13085 (1941).
\(^3\) American Tobacco Co v. United States, 328 U. S. 781 (1946).
\(^4\) Legal expenses were estimated at more than $1,000,000. *Business Week*, Nov. 8, 1941, p. 18.
\(^5\) On the use of the information rather than grand jury indictment see 54 *Yale L. J.* 707 (1945).
\(^7\) Section 1: "Every contract, combination in the form of trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states, or with foreign nations, is hereby declared to be illegal. . . ." Section 2: "Every person who shall monopolize, or attempt to monopolize, or combine or conspire with any
tion accused defendants, in four counts, of conspiracy in restraint of trade, conspiracy to monopolize, attempt to monopolize, and monopolization of the marketing of leaf tobacco and the production and distribution of tobacco products. Before trial, the five smaller companies were severed on pleas of nolo contendere, which subjected them to fines if American Tobacco Company, Liggett & Myers Tobacco Company, and R. J. Reynolds Tobacco Company were convicted.

After a five months' trial, during which evidence on all phases of the tobacco business was introduced, the jury rendered a verdict of guilty on all four counts, and the court imposed on both corporate and individual defendants maximum fines totalling $255,000. The Circuit Court of Appeals for the Sixth Circuit affirmed the convictions in December, 1944. In March, 1945 the Supreme Court granted certiorari, limited to the question whether actual exclusion of competitors was necessary to the crime of monopolization. This question the Court answered adversely to appellants in a decision handed down June 10, 1946, unanimously affirming the judgment of the circuit court of appeals and awarding final victory to the Government in the prolonged court battle.

The basic allegations of the Government's case were that the major

other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations, shall be deemed guilty of a misdemeanor, ..." 26 Stat. 209 (1890), 15 U. S. C. §§1 and 2 (1940).

A two-year investigation of the industry by the Antitrust Division of the Department of Justice preceded the filing of the criminal information. N. Y. Times, July 25, 1940, p. 19, col. 8.

Hereinafter called American, Liggett and Reynolds.

Brief for the United States in Opposition to Petition for Certiorari, p. 4.

This, of course, considerably eased the prosecution's task, permitting it to concentrate on the three undisputed leaders of the industry.


Maximum fine for any single violation of the Act is $5000. No fines were imposed under the third count, the court ruling that the attempt to monopolize was merged in the crime of monopolization. American Tobacco Co. v. United States, 328 U. S. 781, 783. Total fines levied under the other three counts were as follows: American, one subsidiary and four officers, $90,000; Liggett and four officers, $75,000; Reynolds and five officers, $90,000. Record, pp. 6606-7. After the Supreme Court decision, defendants who had pleaded nolo contendere were fined a total of $42,000. P. Lorillard Co., Philip Morris & Co., and Imperial Tobacco Co. each paid $9000; British-American Tobacco Co. and its subsidiary Export Leaf Tobacco Co. together forfeited $9000; and Universal Leaf Tobacco Co. was fined $3000. Business Week, Oct. 5, 1946, p. 54.


American Tobacco Co. v. United States, 328 U. S. 781 (1946). Justices Reed and Jackson did not participate in the decision. Justice Frankfurter concurred but would have enlarged the scope of certiorari to permit consideration of alleged errors in selection of the jury. Justice Rutledge concurred but expressed no opinion on the issue of possible multiple punishment under counts of conspiracy in restraint of trade, monopolization, and conspiracy to monopolize.
tobacco companies had engaged in a conspiracy to control and manipulate the prices, conditions and instrumentalities of the marketing of leaf tobacco and the manufacture and distribution of cigarettes and other products, eliminating competition among themselves and suppressing the competition of others, that this constituted a conspiracy in restraint of trade, a conspiracy and attempt to monopolize, and, since it succeeded, a monopolization of the industry. By monopolization the prosecution meant the intentional acquisition and maintenance by defendants, as a group, of power to dominate, control and exclude others from the industry. The evidence, for the most part circumstantial, which was held by the circuit court of appeals sufficient to sustain the verdict of the jury, may be briefly reviewed.

Dominant position of the Big Three. Ever since their emergence from the dissolved tobacco trust in 1911, American, Liggett and Reynolds have been the largest companies in a steadily expanding tobacco industry which has become predominantly a cigarette industry.

26 Record, pp. 19, 25, 28, 32.
27 Record, pp. 25-6, quoted in American Tobacco Co. v. United States, 328 U. S. at 784 n. 3.
28 American Tobacco Co. v. United States, 147 F. 2d at 112.
29 In United States v. American Tobacco Co., 221 U. S. 106 (1911), the Supreme Court declared the old American Tobacco Company an illegal combination under Sections 1 and 2 of the Sherman Act and ordered its dissolution. The decree of dissolution divided the assets among fourteen corporations, with American, Liggett and Reynolds receiving large holdings. United States v. American Tobacco Co., 191 Fed. 371 (C. C. S. D. N. Y. 1911). See generally Jones, THE TRUST PROBLEM IN THE UNITED STATES, 124 et seq. (1922); Cox, COMPETITION IN THE AMERICAN TOBACCO INDUSTRY (1933). The circuit court's permanent injunction forbade defendants "From continuing or carrying into further effect the combination adjudged illegal in this case, and from entering into or forming any like combination or conspiracy, the effect of which is or will be to restrain commerce in tobacco or its products ... or to prolong the unlawful monopoly of such commerce obtained and possessed by the defendants, as adjudged herein.... 2. By making any express or implied agreement or arrangement together or one with another like those adjudged illegal in this case, relative to the control or management of any of said 14 corporations, or the price or terms of purchase, or of sale, of tobacco or any of its products, or the supplies or other products dealt with in connection with the tobacco business, or relative to the purchase, sale, transportation, or manufacture of tobacco, or its products or supplies, or other products dealt with as aforesaid, by any of the parties hereto, which will have a like effect in restraint of commerce... to that of the combination, the operation of which is enjoined in this cause.... " United States v. American Tobacco Co., 191 Fed. at 428-9. The Government might have proceeded against the Big Three in 1940 for a violation of this decree, instead of bringing the prosecution under the Sherman Act. But such a proceeding for contempt of the decree would not have included Philip Morris & Co., Imperial Tobacco Co. and Universal Leaf Tobacco Co., would have necessitated proof of a combination and of arrangements "like the ones in the 1911 case, and would have been of limited value as a precedent.
30 American Tobacco Co. v. United States, 328 U. S. at 791 n. 7. In 1911 565 million pounds of leaf tobacco were used in the manufacture of all tobacco products in the United States. In 1939 the figure was 885 million pounds; in 1945, 1.3 billion pounds. Of this leaf tobacco cigarettes consumed 7% in 1911, 57.5% in 1939, and 72% in 1945. ANN. REP. ON TOBACCO STATISTICS (U. S. Dep't Agric. 1937-46). In value as well as volume cigarettes outstripped other tobacco prod-
These companies manufactured over 68% of the cigarettes, 63% of the smoking tobacco, and 44% of the chewing tobacco produced in the United States in 1939. During the decade 1930-39 their percentage of domestic cigarette production dropped from 91% to 68%, but their volume of production increased from 106 to 123 billion cigarettes, and no outside competitor ever sold half as many cigarettes as the smallest of the Big Three.

In financial strength, as in production, American, Liggett and Reynolds tower over actual and potential competitors. In 1939 the tangible assets of American amounted to $237,130,931, of Liggett, $181,453,497, of Reynolds, $176,709,822. Their combined tangible and intangible assets in that year exceeded $649,000,000. Their net earnings for 1939, after taxes, were as follows: Reynolds, $26,645,455; American, $26,427,934; Liggett, $20,705,549. Their tremendous expenditures for advertising (over $40,000,000 in 1939) warn new or potential entrants of the costly outlays necessary to compete for sales. Their three year stocks of leaf tobacco, valued at over $100,000,000 for each company, are heavy overhead items, but they assure independence of the farmers' market in any one year.

The strategic position of these three dominant manufacturers is enhanced by the nature of the markets in which they deal. Their chief raw material is bought from thousands of tobacco farmers in over 100 auction markets throughout the South. Leaf tobacco is perishable unless redried, and the farmers have no facilities for redrying; they

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<tr>
<th>Year</th>
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<th>Liggett</th>
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<tr>
<td>1930</td>
<td>87.7%</td>
<td>74.3%</td>
<td>62.6%</td>
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<tr>
<td>1931</td>
<td>88.7%</td>
<td>71.9%</td>
<td>65.6%</td>
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<tr>
<td>1932</td>
<td>78.7%</td>
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<td>66.9%</td>
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<td>1933</td>
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<tr>
<td>1934</td>
<td>77.5%</td>
<td>63.6%</td>
<td>73.2%</td>
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<tr>
<td>1935</td>
<td>75.7%</td>
<td>62.1%</td>
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21 American Tobacco Co. v. United States, 328 U. S. at 796. The best available figures for a period of years do not show the proportion of total production of tobacco products attained by the three companies, but only the share of the three leading cigarette brands—Lucky Strike (American), Camel (Reynolds), Chesterfield (Liggett)—in the national consumption picture:

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American Tobacco Co. v. United States, 328 U. S. at 795.

23 American Tobacco Co. v. United States, 147 F. 2d at 100. By way of comparison, in 1939 the total assets of P. Lorillard Co. were $57,500,000, and those of Philip Morris & Co. were $37,100,000. Moody's Industrials 2480, 2684 (1946) and prior years.

24 Ibid.

25 American Tobacco Co. v. United States, 328 U. S. at 797.

26 Ibid. at 799.

27 Id. at 800.
must sell their tobacco in the season in which it is raised or lose it. With the nation wide popular demand, maintained by advertising, for Lucky Strikes, Chesterfields and Camels, storekeepers of all types as a practical matter must handle these and similar brands. They cannot hold out for higher profit margins or resist manufacturer interference in their business.

The marked superiority of the Big Three in resources and production and their concentrated power in relation to sources of supply and channels of distribution carried with it ample opportunity for abuse. The jury verdict indicates that the opportunity was utilized in both major segments of the tobacco industry.

Leaf tobacco marketing. In the auction markets where farmers sell their tobacco, buyers representing American, Liggett and Reynolds are accorded the respect their quantity purchases warrant. These companies together purchased between 50% and 80% of the flue-cured tobacco bought by domestic producers (about one-half the annual crop is exported, chiefly to England), between 60% and 80% of all burley tobacco, and the greater part of the Maryland tobacco crop. From the practices of the companies, as the largest buyers on the markets and as members of the Tobacco Association of the United States, the jury inferred that a conspiracy to fix prices and “rig” the markets existed.

None of the Big Three would buy on any market unless the others were also represented. Since a market without their presence would be a failure, the opening of new markets depended on their unanimous consent, arrived at by consultation. Market regulations were laid down by the Tobacco Association in which they, but not the farmers, were represented. In separate instructions to their buyers the companies set top prices or price ranges for the various grades of tobacco, and in practice these maximum prices were the same for all of them. Thus, under an auction custom awarding sales to the first of the bidders, company buyers often bid for leaf at the understood ceiling price before an opening price was announced, thus establishing prior claim to the tobacco at that price. Similarly, buyers bid ahead on baskets farther down the line, and without mention of price the auctioneer awarded them these baskets at the understood ceiling.

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29 Id. at 799.  30 Id. at 804.  31 Id. at 799.
29 Id. at 799.  30 Id. at 804.  31 Id. at 799.
32 This Association, composed of manufacturers, buyers, warehousemen and others connected with the industry, but excluding farmers, sets the dates for opening the flue-cured markets and passes regulations on sales, etc. Id. at 800.
32 This Association, composed of manufacturers, buyers, warehousemen and others connected with the industry, but excluding farmers, sets the dates for opening the flue-cured markets and passes regulations on sales, etc. Id. at 800.
33 Id. at 800. The foreign purchasers likewise would not participate without the presence of the Big Three. Id. at 801.
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34 Id. at 801.  35 Id. at 800.  36 Id. at 801.
34 Id. at 801.  35 Id. at 800.  36 Id. at 801.
35 Id. at 801.  36 Id. at 802.
Restriction of competition was also accomplished in other ways. Each company formulated distinctive grades of tobacco which it alone purchased, and the other companies did not compete for these grades. Before the market seasons opened each company separately informed its buyers what percentage of the flue-cured, burley and Maryland tobacco crop it wished to purchase, and its buyers limited their acquisitions on each market to this percentage. However, competition was not so completely eliminated that a company could buy its tobacco at any price it wished. Each company was much more concerned that all three should pay the same price for the same quality tobacco than that any particular prices be maintained. Where one or two of them had secured their percentages on a market or were not interested in particular leaf offerings, their buyers nevertheless would enter the bidding to force the others up to their ceiling prices. Company supervisors, through instructions to buyers on prices and percentages, strove to maintain the same prices and grades and to achieve stability on all markets.

During the early Thirties when ten-cent cigarettes were gaining rapidly at the expense of the standard or fifteen-cent brands, the Big Three began making large purchases of the cheaper leaf used in the manufacturer of ten-cent cigarettes. This tobacco was not substituted for the more expensive grades in Luckies, Chesterfields and Camels, and no explanation of its use was offered. The Government claimed that the purchases evidenced a conspiracy to deprive the markers of ten-cent cigarettes of their chief raw material and by increasing their tobacco costs raise their cigarette prices or otherwise choke off their competition.

Sale of tobacco products. References to the “fierce competition” in the tobacco industry describe the strenuous efforts of cigarette manufacturers to outsell their rivals by superior sales promotion campaigns. There is certainly no competition in price. The list prices and discounts of American, Liggett and Reynolds were practically identical from 1923 and absolutely identical from 1928 to the time of trial. Between 1928 and 1940 only seven price changes were made by the three companies and they were identical in amount. Although the changes were not announced by all companies on the same day, they

The differences between these grades were distinguishable by highly trained special buyers but they did not accord with the government grades and were “in reality so minute as to be inconsequential.” American Tobacco Co. v. United States, 328 U. S. at 802.

"Ibid."

"Id. at 803." "Id. at 802." "Id. at 803." "See infra p. 145."

"American Tobacco Co. v. United States, 328 U. S. at 803-4."

"A modern survey states: “Competition is limited to promotion technique since all major producers adhere to a single price schedule.” STANDARD & POOR'S INDUSTRY SURVEY: TOBACCO, Part II, T4-15, April 21, 1944."

"American Tobacco Co. v. United States, 328 U. S. at 804."

"Ibid."

"Ibid."
were in effect simultaneous, because after the announcement by one company and before the other companies had followed suit they refused to sell to dealers at their unchanged price.\textsuperscript{50}

The most serious misstep of the Big Three, one which revealed their monopoly power and precipitated their difficulties with the ten-cent cigarettes, was the price increase of 1931. In that year, with their share of total cigarette production over 90\%, leaf tobacco costs at their lowest and depression gripping the country, the companies, Reynolds leading, raised the list price of cigarettes from $6.40 to $6.85 per thousand.\textsuperscript{51} No economic justification for this move was demonstrated.\textsuperscript{52} Although their sales volume dropped greatly, combined net profits exceeded $100,000,000.\textsuperscript{53} It was one of the three best years in their history.

Since the demand for cigarettes is comparatively inelastic, as sales of Lucky Strikes, Camels, and Chesterfields declined sales of ten-cent cigarettes increased until in November, 1932 they had absorbed 23\% of the national market.\textsuperscript{54} Counterattack by the Big Three followed. Two price cuts in early 1933 necessitated sales of Camels and Lucky Strikes at a loss but brought victory over the ten-cent brands.\textsuperscript{55} By May, 1933 these brands were making only 6.4\% of the total cigarette sales.\textsuperscript{56} In January, 1934 the price of the Big Three brands was raised from the low of $5.50 to $6.10 a thousand.\textsuperscript{57} The only subsequent changes were increases in 1937 and 1940, the latter occasioned by an advance in the federal tax rate.\textsuperscript{58}

In both the elimination of price competition among themselves and the concerted assault on their lower-priced competitors, the three leading manufacturers found it necessary to control the prices at which their products were sold by distributors. They insisted on identical wholesale and retail prices for their brands, based on equality of factory

\textsuperscript{50} Id. at 808.
\textsuperscript{51} Id. at 805. The net price, after deducting discounts and federal tax of $3.00 per thousand, was increased from $2.64 to $3.04.
\textsuperscript{52} Ibid. Reynolds' president stated that it was “to express our own courage for the future and our own confidence in our industry.” The president of American saw an opportunity to make money and felt impelled to follow Reynolds in order to have the same funds for advertising. Liggett's officials thought the increase was a mistake but did not wish to be deprived of the resources for greater advertising. \textit{Ibid}.
\textsuperscript{53} Id. at 806.
\textsuperscript{54} Ibid.
\textsuperscript{55} Id. at 806-7. The first cut, in January, 1933, was from $6.85 to $6.00 a thousand. The second, in February, 1933, lowered the list price to $5.50 a thousand. Liggett had to curtail all expenses, especially advertising, in order to sell Chesterfields at this price. \textit{Ibid}.
\textsuperscript{56} Id. at 807.
\textsuperscript{57} Ibid.
\textsuperscript{58} Id. The cigarette tax, which had been $3.00 a thousand since 1919, was raised to $3.25, effective July 1, 1940. A further increase to $3.50 was made on Nov. 1, 1942. \textit{Ann. Rep. on Tobacco Statistics} 50 (1946).
prices. Finding that a differential of not more than three cents a pack between their brands and the ten-cent cigarettes would enable them to outsell the latter, they demanded that retailers maintain this differential, either by raising the price of the cheaper cigarettes or charging less for the standard brands. The evidence that Big Three representatives acted together in enforcing this policy was one of the few direct proofs of collusion in the case.

Another set of circumstances justifying the inference of conspiracy occurred at the height of the price war, when American, Liggett and Reynolds sought to lower the retail price of their cigarettes to ten cents per pack. Before the factory price cut of February 11, 1933 was announced to the trade, the Great Atlantic & Pacific Tea Company prepared posters advertising new retail prices and on February 10th sent out instructions to its 15,000 stores to charge ten cents for the leading brands, effective the next day. Allegedly this action was taken without advance notice from any of the manufacturers and solely on the basis of unconfirmed rumors of the trade.

In order to control distributors' prices the Big Three rewarded cooperating dealers with the privilege of purchasing direct from the manufacturer and gave them discounts, advertising displays, cash subsidies and free goods. The companies withdrew or withheld these benefits from recalcitrant dealers and subsidized competing dealers as price cutters to maintain the price parity of the leading brands and enforce the three-cent price differential.

To show opportunity for communication and agreement the Government presented evidence of the activities of the Tobacco Merchants Association and the companies' heavy financial contributions to it. Representatives of the three manufacturers were in constant touch with the director of the Association, participated in its meetings and worked through it for certain common objectives, such as defeating proposed state cigarette taxes.

American Tobacco Co. v. United States, 328 U. S. at 808; American Tobacco Co. v. United States, 147 F. 2d at 105.
American Tobacco Co. v. United States, 328 U. S. at 807.
American Tobacco Co. v. United States, 147 F. 2d at 106.
Ibid.
Ibid.

Cigarette manufacturers have not fixed the retail prices of their products under state resale price maintenance statutes. Prior to the passage in 1937 of the Miller-Tydings Amendment to the Sherman Act, 26 Stat. 209 (1890), as amended, 50 Stat. 693 (1937), 15 U. S. C. §1 (1940), resale price maintenance in interstate commerce was held a violation of federal antitrust law. Dr. Miles Medical Co. v. Park & Sons Co., 220 U. S. 373 (1911). Under the Miller-Tydings Amendment the tobacco companies can lawfully fix retail and wholesale prices in accordance with state statutes, but in spite of continual appeals from tobacco distributors they have not done so. See, for example, unanimous resolution of the convention of the National Ass'n of Tobacco Distributors, N. Y. Times, Mar. 20, 1946, p. 30, col. 8.

American Tobacco Co. v. United States, 328 U. S. at 808.
Ibid.
American Tobacco Co. v. United States, 147 F. 2d at 119.
Viewing the evidence as a whole, the jury found that American, Liggett and Reynolds had wielded their tremendous power in concert to undermine the farmers' bargaining position, to fix prices of both leaf tobacco and tobacco products, to restrain competition among themselves, to injure the business of competing manufacturers and to coerce and control the distributors of cigarettes and allied tobacco products.

The legal questions. Although from a record of over 10,000 pages innumerable assignments of error could be extracted, the issues directly related to antitrust law were quite limited in number, and all but one were conclusively settled by the circuit court of appeals.

Appellants contended strongly that the verdict was not supported by the evidence, that there was no proof of violations of the Act. The question for the circuit court of appeals was whether there was substantial evidence from which the jury properly could have found or inferred, beyond a reasonable doubt, that defendants were guilty. The court's answer was a clear affirmative. Admittedly no express or formal agreement to restrain trade or monopolize was shown, but such evidence is rarely available and is not essential to a criminal conspiracy case. Proof of an agreement, combination or conspiracy was, as the trial court instructed, an "essential element" of the crimes charged, but, in the words of the appellate court, "The agreement may be shown by a concert of action, all the parties working together understandingly, with a single design for the accomplishment of a common purpose," and "... the essential agreement, combination and conspiracy in violation of the Sherman Act may be implied from, or found in a course of dealing or other circumstances, as well as through an exchange of words."

The Supreme Court went even further:

"This particular conspiracy may well have derived special vitality, in the eyes of the jury, from the fact that its existence was established, not through the presentation of a formal written agreement, but through the evidence of widespread and effective conduct on the part of petitioners in relation to their existing or potential competitors."
Given the fact that a conspiracy existed, was it the type of combination condemned by the Sherman Act? As to a conspiracy in restraint of trade under Section 1 of the Act there could be little room for doubt. The companies had combined to fix leaf tobacco and cigarette prices. Price fixing is per se a restraint of trade, whether the prices fixed are reasonable or unreasonable, rigid or flexible.\footnote{United States v. Socony-Vacuum Oil Co., 310 U. S. 150 (1940); United States v. Trenton Potteries, 273 U. S. 392 (1927).} The companies had acted together to control resale prices and distribution of tobacco products. Such schemes, even when indulged in by a single manufacturer and his distributors, are illegal restraint of trade.\footnote{United States v. Bausch & Lomb Optical Co., 321 U. S. 707 (1944); United States v. Masonite Corp., 316 U. S. 265 (1942); Ethyl Gasoline Corp. v. United States, 309 U. S. 436 (1940); Federal Trade Comm'n v. Beech-Nut Packing Co., 257 U. S. 441 (1922); United States v. A. Schrader's Sons, 252 U. S. 85 (1920).}

The two counts charging conspiracy to monopolize and monopolization in contravention of Section 2 presented the only novel question. The trial court defined the term "monopolization" as "the joint acquisition or maintenance by the members of a conspiracy formed for that purpose, of the power to control and dominate interstate trade and commerce in a commodity to such an extent that they are able, as a group, to exclude actual or potential competitors from the field, accompanied with the intention and purpose to exercise such power."\footnote{American Tobacco Co. v. United States, 147 F. 2d at 109-12.} The circuit court of appeals approved this definition and held the evidence warranted a jury finding that the Big Three, in combination, had power to exclude competitors and the intent to exercise that power.\footnote{American Tobacco Co. v. United States, 328 U. S. at 810.} Under the limited review granted by the Supreme Court this was the only issue before it, and the Court completely agreed that neither proof of actual exclusion nor of exertion of power to exclude existing or potential competitors was essential to the crime of monopolization.\footnote{"This acquisition placed the Holding Company in a position of dominating control not only over two great competing interstate railroad carriers but also over two great competing coal companies. . . . That such a power, so obtained, regardless of the use made of it, constitutes a menace to and an undue restraint upon interstate commerce within the meaning of the Anti-Trust Act, has been frequently held by this court." United States v. Reading Co., 253 U. S. 26, 57 (1920); "It is the scope of such combinations and their power to suppress or stifle competition or create monopoly which determines the applicability of the act." United States v. Union Pacific R. R., 226 U. S. 61, 88 (1912); "The mere existence of such a combination and the power acquired by the holding company as its trustee, constituted a menace to, and a direct restraint upon, that freedom of commerce which Congress intended to recognize and protect, and which the public is entitled to have protected." Northern Securities Co. v. United States, 193 U. S. 197, 327 (1904); accord, United States v. Socony-Vacuum Oil Co., 310 U. S. 150, 226 n. 59 (1940); Harriman v. Northern Securities Co., 197 U. S. 244, 291 (1905); United States v. Aluminum Co. of America, 148 F. 2d 416, 429-32 (C. C. A. 2d).} Although the precise issue had not been previously decided by the Court, language in several earlier cases pointed toward the conclusion reached.\footnote{"United States v. Socony-Vacuum Oil Co., 310 U. S. 150, 226 n. 59 (1940); Harriman v. Northern Securities Co., 197 U. S. 244, 291 (1905); United States v. Aluminum Co. of America, 148 F. 2d 416, 429-32 (C. C. A. 2d).}
THE AMERICAN TOBACCO COMPANY CASE

THE THEORY OF MONOPOLISTIC COMPETITION

The full significance of the judicial outcome in the American Tobacco Company case cannot be understood except in relation to economic theory, for the whole purpose of the Sherman Act is to preserve and protect a particular form of economic system, namely, free competitive capitalism.82

Statement of the theory. Under free competition supply and demand for a commodity are brought into equilibrium at a market price which encourages full production by each competitor, the most efficient scale of production in his enterprise and economic benefits to society as a whole. Such competition, however, assumes two vital conditions—a large number of sellers, and a standardized commodity sold in a single market.83 Under these conditions, perhaps exemplified in the grain market, the individual seller produces on the assumption that his entire output can be disposed of at the market price. For him market price is a given quantity, demand is virtually unlimited, and his output is expanded until the cost of producing one more unit equals the market price. If the price which equates supply and demand yields high profits, new competitors enter the industry, and a new equilibrium price and a more productive use of resources follow.

So much for the familiar learning of pure competition, i.e., competition without monopoly elements. Suppose, however, that the two fundamental conditions do not exist, that there are only a few sellers and their products are differentiated. Professor Chamberlin and others84 have demonstrated that the resulting situation, which Chamberlin calls monopolistic competition, is quite different from pure competition, and


83 "The end sought was the prevention of restraints to free competition in business and commercial transactions which tended to restrict production, raise prices or otherwise control the market to the detriment of purchasers or consumers of goods and services, all of which had come to be regarded as a special form of public injury." Apex Hosiery Co. v. Leader, 310 U. S. 469, 493 (1940).

"it is no longer safe even in theory to assume that its social results are salutary."

With only a few sellers the individual producer can no longer ignore the effects of his policies on the market price. He must take into account not only his direct influence, through the price he sets on his goods and the quantity he puts on the market, but also his indirect influence on price, through the effect of his action on the policies of the other sellers. For example, a price cut may appear advantageous to one cigarette manufacturer in view of the rival's present policy, but he must recognize that his reduction will be met by his rival, and in the end each will be selling approximately the same share of a less valuable market.

"To the argument that if he did not cut his rival would, the answer is that his rival would not for the same reason that he does not. If each seeks his maximum profit rationally and intelligently ... no one will cut, and although the sellers are entirely independent, the equilibrium result is the same as though there were a monopolistic agreement between them."

Assuming immediate response by one seller to another's move, and a minimum of uncertainty on the part of one as to the other's probable reaction, each will sell at the same price and it will be a monopoly price. The explanation is that each producer is attempting to maximize his profits under conditions which require him to consider his total influence on price. No agreement, tacit or otherwise, is necessary.

The second requirement of pure competition is a standardized commodity sold in a single market. With no basis for buyer preference of one producer's commodity over another, demand for each seller's product is highly elastic; an increase in his price will send his buyers to other sellers. But where products are differentiated, either actually or in the minds of buyers, the situation is more nearly that of competing

89 CHAMBERLIN, supra note 83, at 30-55.
87 This assumes either (1) substantially inelastic total demand, that is, a reduction in price brings only a small increase, or no increase in total consumption, or (2) an elastic demand for cigarettes but a smaller total profit for manufacturers on the increased volume than on the old volume at a higher price. Actually, inelasticity of demand is characteristic of the tobacco industry because of habit-forming tendencies and brand promotion and devotion.
88 CHAMBERLIN, supra note 83, at 48.
89 Id. at 31.
90 "Commodity" covers both characteristics of the product itself and conditions surrounding its sale, including quality, design, packaging, service, location of sale, etc. Id. at 7-8, 56.
91 BURNS, supra note 84, at 3.
92 A general class of product is differentiated if any significant basis exists for distinguishing the goods of one seller from those of another. CHAMBERLIN, supra note 83, at 56.
For example, American Tobacco Company has a monopoly of Lucky Strike cigarettes, but Lucky Strikes compete with other brands of cigarettes, with other tobacco products, such as cigars, and to a much smaller extent with other substitutes, such as candy and chewing gum. Under monopolistic competition a seller's ability to charge a monopoly price is limited only by the presence of substitutes and the elasticity of demand for his product. In the case of Lucky Strikes these factors prevent sale at a higher price than other leading brands, but price differentials exist in the face of standard quality in aspirin, soda and other drugs. And uniformity of price among cigarette brands is not indicative of pure competition, where neither of the conditions of such competition are present.

Advertising and similar promotion are crucial to product differentiation. They inform buyers of real and impress them with fancied differences in commodities. The theory of monopolistic competition recognizes that advertising may increase the demand for a particular brand, decrease the elasticity of that demand, and raise the total demand for products of the same general class. But the costs of such promotion and the inelasticity of demand achieved mean that prices are inevitably higher than under pure competition. Of course, high prices do not necessarily produce monopoly profits; heavy production and selling costs and development of excess productive capacity may reduce earnings to competitive levels. However, advertising, which raises costs, at the same time increases the possibility of monopoly profits by partially protecting the field against the incursions of new competition.

Although both types of competition have the same driving force—maximization of profits—different basic conditions bring about higher prices, lower production, less effective utilization of resources and less flexible adjustment to changes under monopolistic than under pure competition. And to these obvious economic disadvantages must be added a tendency to accentuate the business cycle and to decrease employment opportunities.

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93 Id. c. 5.
94 Id. at 117-29.
95 Id. at 166. That is not to say, however, that monopolistic competition with advertising may not produce a cheaper product than monopolistic competition without advertising, through possible economies in large scale production. Id. at 130-66.
96 Selling costs are costs which alter the demand curve for a product. Production costs are those which do not. Id. at 123.
97 Id. at 88, 100-14.
98 Id. at 173. This tendency was noted by the Supreme Court in the tobacco industry. American Tobacco Co. v. United States, 328 U. S. at 797 (1946).
99 With the uniformity and stability of administered prices under monopolistic competition, adjustments are made largely through changes in production. During the downward phase of a business cycle manufacturing prices tend to be relatively inflexible, output falls off, employment drops, and additional shock is thrown on the more flexible parts of the economy, such as agriculture. Means, Industrial Prices and Their Relative Inflexibility, Sen. Doc. No. 13, 74th Cong., 1st Sess. (1935).
Application to the tobacco industry. An economic theory which analyzes competition containing monopoly elements is much more realistic than the old distillation of pure competition and pure monopoly, but in actual fact no market is without monopoly elements, and the economists have not yet furnished us tests to measure with accuracy the degrees of monopoly and its harmful results to society. In the absence of such tests and the complete data necessary for such measurement, only rough estimates are possible, but the extent to which the fundamental conditions of pure competition have been replaced and the history of operations in the tobacco industry indicate a rather high proportion of monopoly in the compound of monopolistic competition undeniably present therein.

The industry is certainly one of huge size and a limited number of producers. Six firms averaged 94.2% of the total cigarette sales from 1931 through 1939, and estimates of production since that date reveal no substantial change in this figure. Concentration of business in a few companies is also characteristic of the other branches of the industry, although less marked in cigar manufacturing. Cigarette prices have been uniform for all major brands and price stability has been achieved. Each company takes into account the effect of its

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100 American, Reynolds, Liggett, Philip Morris & Co., P. Lorillard Co. (Old Golds), Brown & Williamson Tobacco Co. (Raleighs).
101 American Tobacco Co. v. United States, 328 U. S. at 794. Peak year was 1931 with 98.3% and lowest year was 1939 with 91.5% of total domestic production. Ibid.
102 Estimates for just the leading brands of these six firms show an average of 82.55% of total cigarette sales in the years 1940-45. The comparable figure for 1931-39 was 83.96%. STANDARD & POOR'S INDUSTRY SURVEY: TOBACCO, Part II, T4-5, April 10, 1946. In 1946 Lucky Strikes, Camels and Chesterfields comprised 73.2% of all cigarettes produced. N. Y. Times, Jan. 31, 1947, p. 28, col. 6.
103 American, Liggett, Reynolds and Lorillard produced 74% of the smoking tobacco and 70% of the chewing tobacco in 1934, but only 15% of the cigars. In 1934 United States Tobacco Co., American Snuff Co. and George W. Helme Co. made 95% of domestic snuff sales. In the combined chewing and smoking tobacco and snuff branches the largest four enterprises produced 64% and the largest eight 84% of the product in 1935. In cigars, however, the largest four produced only 39% and the largest eight 51% of the total. Report of the Smaller War Plants Corp., Economic Concentration and World War II, SEN. Doc. No. 206, 79th Cong., 2d Sess. 227-32 (1946). The above report lists the tobacco industry as the second most concentrated industry in America. Concentration is measured in three ways: (1) Employment—percentage of all workers employed by concerns with more than 500 employees (tobacco industry, 78.3%); (2) Production—proportion which value of different tobacco products manufactured under conditions where four largest producers of each product manufactured from 75% to 100% of that product bears to the total value of all products (tobacco industry, 86.4%); (3) Sales—percentage of total volume of sales made by corporations with assets of $50,000,000 and over (tobacco industry, 73.5%). Id. at 66-75.
104 See supra pp. 144-145.
105 From 1930 to 1946 there were only nine changes in the price of standard cigarette brands, and two were due to increased federal tax rates. Net factory price, after discounts and excluding federal tax, remained the same from 1931 to 1933, from 1934 to 1937, and from 1937 to 1941, when OPA action prevented change until 1946. OPA Revised Price Schedule No. 62—Cigarettes (as amended), 7 FED. REG. 1332, 1836, 2132, 2242, 8948 (1942), 9 FED. REG. 2667 (1944), 11 FED.
price on its rivals' policies, prices move together, and product prices are higher than under pure competition—witness the 1931 price increase. Although leaf tobacco prices have fluctuated widely there can be little doubt that their general level is lowered by reason of the small number of buyers in the market.

Differentiation of product, chiefly by advertising, has reached a high peak in the tobacco business. Advertising has proved its effectiveness in shifting demand among particular brands; how much of a factor it has been in the growth of total tobacco consumption is not clear. With continually expanding consumption, however, large scale promotion may attract new smokers to one producer's brand without cutting seriously into existing sales volume of a competing brand and inviting uneconomic retaliation; this has probably been a factor in the huge size of cigarette advertising budgets. Although refined differentiation and energetic promotion of tobacco products undoubtedly have increased the natural

RES. 4609 (1946); ANN. REP. OF TOBACCO STATISTICS (U.S. Dept't Agric. 1937-46); STANDARD & POOR, supra note 102, at T4-3; TOBACCO, Oct. 10, 1946, p. 3. Oct. 17, 1946, p. 3. A contributing factor to this stability of price has been the companies method of accounting for leaf costs on the basis of a three-year average. This reduces the tendency of fluctuating leaf costs to cause changes in cigarette prices. Cox, COMPETITION IN THE AMERICAN TOBACCO INDUSTRY 191 (1933).

For example, in mid-1946 after OPA's demise, Liggett raised the price of Chesterfields 22 cents a thousand, effective August 1, 1946. The other manufacturers did not follow. On August 6th Liggett rescinded the price increase. N.Y. Times, July 31, 1946, p. 29, August 7, 1946, p. 29.

Monopolistic competition works the same way in a market with few buyers and many sellers as in one with few sellers. If one buyer considers bidding higher to obtain more leaf he knows his rivals will bid high also and each will obtain in the end about the same share, but at a higher price. So each buyer restrains his bidding and without agreement among the buyers the price is lower than a purely competitive one.

See ANNUAL REPORT OF THE AMERICAN TOBACCO COMPANY 14 (1945): "The record proves that the amount of money spent on cigarette advertising is modest in relation to the sales results achieved." Average advertising expenses for Lucky Strikes from 1934 to 1943 were 12.7 cents per 1,000 cigarettes. Ibid. Evidently American was able to hold or improve its position during this period with a smaller advertising budget than Reynolds or Liggett. For relative sales trends of major cigarette companies, 1934-45, see STANDARD & POOR, supra note 102, at T4-4.

Evidently American was able to hold or improve its position during this period with a smaller advertising budget than Reynolds or Liggett. For relative sales trends of major cigarette companies, 1934-45, see STANDARD & POOR, supra note 102, at T4-4.

Cox, supra note 105, at 222-5. Standard & Poor suggest three reasons for the constant growth of tobacco consumption—habit forming tendency of its use, more rapid expansion of adult population than total population, and long term rising trend of consumer incomes. Over the course of a business cycle total tobacco consumption shows a striking relation to fluctuations in the national income. STANDARD & POOR, supra note 102, at T4-1.

Size of cigarette advertising budgets is indicated by the estimate that from 1939 to 1942 the tobacco industry spent an average of approximately $40,000,000 annually for national advertising through newspapers, magazines, farm journals and radio broadcasting. BORDEN, TAYLOR AND HOWE, NATIONAL ADVERTISING IN NEWSPAPERS 63 (1946). During the above period network radio climbed to 42% of the total expenditure, newspapers dropped sharply to 33% and magazines increased slightly to 23%. Id. at 44. In 1940 the cigarette industry as a whole expended 11.3% of total revenues on advertising; only two industries, drugs and cereals, spent more. Report of the Smaller War Plants Corp., supra note 103, at 231.
inelasticity of demand for these products, the outstanding contribution of such promotion to monopoly in the industry has been in the exclusion of potential competition. This is recognized in the frank statement of a recent survey:

"The chief barrier to new competition is found in the large advertising expenses required to establish any brand in volume.... The large capital investment in inventory and the sizable promotional expenditures required to launch a new brand promise that the cigarette market, as far ahead as can be seen, will continue to be divided among the existing companies."1

In a major manufacturing industry characterized by few producers, wide spread differentiation of product, steadily rising production and serious obstacles to potential competition the existence of monopoly profits would not be surprising. From 1912 to 1930 the return on book value of net investment of American, Liggett, Reynolds and Lorillard averaged 12.4%, varying between a low of 9.52% (1914) and a high of 15.95% (1930).114 Reynolds led the field with a return of almost 20% for the period.115 The ratio of net earnings (after taxes) to net worth for the same companies from 1931 to 1946 averaged 11.56%, with extremes of 8.44% in 1945 and 14.28% in 1931.116 Including Philip Morris with the above four firms increases the sixteen-year average to 12.98%.117 The ability of the large tobacco companies to earn handsome profits compares most favorably with the record of other American manufacturers118 and tobacco distributors.119

112 Standard & Poor, supra note 102, at T4-4. Size of investment in inventory is illustrated by the fact that of Liggett's total assets of $293,400,000 in 1945, $253,300,000 or 86.34% was inventory. Good will was listed as a $1 asset, however. Moody's Industrials 2439 (1946).

113 Of the 45 years from 1900 to 1945 there have been only 10 in which the amount of leaf tobacco processed has not shown an increase over the preceding year. And from 1920 to 1945 per capita consumption of cigarettes rose every year except four—1930, 1931, 1932, 1938. Ann. Rep. of Tobacco Statistics (1937-46).

114 Cox, supra note 105, at 272. Book value of net investment is total of bonds, stocks and surplus. Earnings are after taxes. Source of statistics was annual reports of the companies. Id. at 270.

115 From Moody's Industrials 1957, 1970, 2439, 2480 (1946), and prior years. The low rate of return in 1945 was probably due to OPA ceilings and rising tobacco costs. Earnings jumped to 10.65% of net worth for the four firms in 1946.

116 Moody's Industrials 2684 (1946), and prior years. The 1931-46 mean ratio of earnings to net worth for each of the five companies was as follows: Philip Morris, 18.62% (1933-46 aver.); Reynolds, 15.63%; Liggett, 12.90%; American, 10.67%; Lorillard, 7.00%. Ibid.

117 A study of 2,046 manufacturing corporations, responsible for one-half American manufacturing, showed an average rate of return (before federal taxes) on capitalization (excluding funded debt) from 1919 to 1928 of 10.8%. The rate of return for 23 tobacco corporations was 14.2%, for 17 bakery companies 16.8%, for 16 canned goods companies 13.8%, for 111 paper firms 9.6%, and for 23 meat packing corporations 1.9%. Epstein, Industrial Profits in the United States 242.

118 During the years 1929-35 the rate of return on investment for 13 tobacco
The existence of monopolistic competition in the tobacco industry, noted by several writers, was implicitly recognized by both sides in the recent antitrust litigation. Under counts of monopolization and attempting to monopolize the Government's information charged:

"In adopting and exercising such methods, means and practices, each defendant has acted with full knowledge that unanimity of action with reference thereto was and would be the policy, intent and practice of the others, that such unanimity of action would necessarily result in drawing to defendant major tobacco companies as a group the power to dominate, control, and exclude others from the aforesaid interstate . . . commerce, has intended such result, and such result has in fact been achieved." And in its reply brief American presented the issue as follows:

"The real question is whether in an industry such as this, the anti-trust laws are violated by uniformity of conduct, where normal business factors cause each company, acting individually, to adopt practices and policies that are, in many instances, similar to those of its competitors."

SIGNIFICANCE OF THE DECISION

Before evaluating the significance of the American Tobacco Company case from the point of view of the three groups most concerned with its meaning and effect—the enforcing agencies, the tobacco manufacturers and the public at large, one assumption which is basic to the remaining discussion should be clearly stated. It is that conditions in the tobacco industry, cannot be naïvely dismissed as the result of a comprehensive but cleverly concealed agreement among the big manufacturers to fix prices, control the market and suppress competition. The lack of evidence of any actual plan or agreement among the policymaking officials of the Big Three suggests that while there was some collusion among company representatives, the practices and policies during the 1937-40 period actually at issue were rather the ordinary

manufacturing corporations averaged 15.8%. The average annual return of tobacco wholesalers and jobbers during this period was 4.43%. On the retail level, chain groceries averaged 16.4%, chain drug stores, 8.29%, and chain tobacco stores lost an average of 1.37% annually. Hearings before the Temporary National Economic Committee, 76th Cong., 1st Sess. 1816-21 (1939).

Arnold, The Bottleneck of Business 34 (1940); Burns, The Decline of Competition 225-8, 383 (1936); Cox, Competition in the American Tobacco Industry 316-24 (1933); Handler, Cases and Other Materials on Trade Regulation 404 n. 80 (1937); Lynch, The Concentration of Economic Power 136 (1946).

Reply Brief of Appellant American Tobacco Co., p. 6. See also Petition for Certiorari of Appellant Liggett & Myers Tobacco Co., pp. 7-8; Petition for Certiorari of Appellant R. J. Reynolds Tobacco Co., pp. 5-7, 10; Brief for the United States in Opposition to Petition for Certiorari, p. 37; Record, pp. 458-9.

Under the federal three-year statute of limitations the defendants could only be convicted for offenses committed between July 24, 1937 and July 24, 1940.
features of an industry characterized by monopolistic competition.

The independent, rational reactions of businessmen in such an environment produce practices and policies strikingly similar or even identical to those of their competitors. While this result may be condemned as economically and socially undesirable, it need not be the outgrowth of criminal conspiracy in the usual sense. Conviction and punishment of the "conspirators" would not alone bring about any appreciable change in business conduct. Undeniably, in the six years since the tobacco companies were first pronounced guilty there has been little outward change. In October, 1946 when American increased the net price of Lucky Strikes from $6.25 to $6.50 per thousand and the other companies followed, Reynolds only raised the price of Camels to $6.48, but this hardly signifies the restoration of price competition to the industry. The enforcing agencies. Entirely apart from its direct effect on the individual and corporate defendants, however, the decision in this case has contributed to the development of federal antitrust law and given new encouragement to the agencies responsible for freeing the channels of interstate commerce from the restrictive pressures of monopoly. The federal courts, the Antitrust Division of the Department of Justice, the Federal Trade Commission, and aggrieved persons are all figures in this enforcement picture. They confront today in every major industry

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2. Any individual or corporation who is injured by a violation of federal antitrust laws may bring a civil action for treble damages, 26 Stat. 210 (1890), 38 Stat. 731 (1914), 15 U. S. C. §15 (1940). An aftermath of the Government's victory over the Big Three was a suit in the federal district court in New York by the Monticello Tobacco Co. against American, Liggett and Reynolds and their officials. Monticello alleged that it had suffered $12,000,000 damages because of defendants' restrictive practices and monopolistic control over tobacco distribution, and it requested treble damages of $36,000,000. N. Y. Times, Aug. 27, 1946, p. 35, col. 4.
striking concentrations of power and production in the hands of a few giant corporations. Such concentration is by nature monopolistic, and unless attack under the Sherman Act can destroy it, competition cannot possibly be effective and cannot be relied on to regulate the economy in the public interest.

In at least three ways the American Tobacco Company case points the way toward renewed assault on this modern form of monopoly. In the first place, the decision means that unanimity of action in industries characterized by monopolistic competition may be a form of "conspiracy" in restraint of trade made illegal by the Antitrust Act. Under broad, settled instructions on criminal conspiracy a jury may easily infer that the features of business conduct paraded before its eyes are wholly attributable to an agreement, combination and conspiracy among corporate officers and representatives. The same inference may be drawn by the judge in a civil suit to enjoin violations of the Act.

Of course, an appellate court may reverse this conclusion as not sustained by the evidence, but Judge McAllister's opinion in the circuit court of appeals demonstrates that he too relies heavily on identity of conduct as proof of conspiracy:

"The identical objectives, the opportunity for communication between appellants in formulating policies for their mutual benefit, their concert of action in other matters in which they were mutually interested, their refusal to participate in buying at the markets unless all three appellant companies were present, the uniformity of list prices of their manufactured products, the identical and (for all practical purposes) simultaneous price increases and price reductions, their insistence on identical list prices, the similar rewards and punishments meted out to dealers by all the appellants in carrying out the same objectives, their policies which, in practice, resulted in their refusal to compete with each other in the field of prices, either in the purchase of leaf tobacco or in the sales of their finished products, are all circumstances . . . from which an agreement on the part of the appellants to act in concert, to the extent and in the manner outlined by the court, could be inferred by the jury beyond a reasonable doubt."

Three Supreme Court cases support the view that uniformity of prices and policies among business competitors may amount to illegal conspiracy. In Cement Manufacturers' Ass'n v. United States defendants testified and argued that uniformity of prices in the industry

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127 Comer, Price Leadership, 7 Law & Contemp. Prob. 61 (1940), suggests this technique for handling the similar problem of price leadership.

128 Section 4 invests federal courts with jurisdiction to prevent and restrain violations of the Act and places on the federal district attorneys, under the direction of the Attorney General, the duty of instituting the necessary proceedings in equity. 26 Stat. 209 (1890), 15 U. S. C. §4 (1940).

129 American Tobacco Co. v. United States, 147 F. 2d at 113.

130 268 U. S. 588 (1923).
was symptomatic of competition, but the Court stated in a dictum: "We realize also that uniformity of prices may be the result of agreement or understanding, and that an artificial price level not related to the supply and demand of a given commodity may be evidence from which such agreement or understanding, or some concerted action of sellers to restrain commerce, may be inferred."\(^{131}\)

The *Interstate Circuit* case\(^{322}\) in 1939 developed further this principle of monopolistic conspiracy. A chain theater operator addressed a letter to eight motion picture distributors proposing price and other restrictions in their contracts with subsequent-run theaters in the operator's territory. Evidence of unanimous acceptance of the restrictions for part of the territory and rejection for other parts, and of strong motives for unanimity of action among the distributors, together with failure of high officials of the distributors to testify, was held sufficient to sustain a finding of conspiracy among the distributors, even though no agreement or communication among them was shown. Justice Stone declared that in the circumstances an actual agreement was not a prerequisite to an unlawful conspiracy. "It was enough that, knowing that concerted action was contemplated and invited, the distributors gave their adherence to the scheme and participated in it."\(^{133}\)

The reasoning of the *Interstate Circuit* case was followed in *United States v. Masonite Corp.*,\(^{324}\) a 1942 decision. Although the restrictive "agency" agreements between Masonite and eight or more manufacturers or distributors of building materials were made separately and independently, the awareness of each manufacturer or distributor that its contract with Masonite was part of a larger arrangement was held sufficient to support a finding of illegal combination and conspiracy.

Certiorari has been granted recently in a case which should clarify the effect of uniformity of prices and practices in antitrust actions.\(^{125}\) Actually the proceeding is not under the Sherman Act but is for review of a Federal Trade Commission order enjoining the cement industry's use of the multiple basing point pricing system as an unfair method of

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\(^{123}\) 306 U. S. at 226; accord, Bigelow v. RKO Radio Pictures, 150 F. 2d 877 (C. C. A. 7th 1945), *rev'd on other grounds*, 327 U. S. 251 (1946); William Goldman Theatres v. Loew's Inc., 150 F. 2d 738 (C. C. A. 3d 1945), *reversing* 54 F. Supp. 1011 (E. D. Pa. 1944): "Uniform participation by competitors in a particular system of doing business where each is aware of the other's activities, the effect of which is restraint of interstate commerce, is sufficient to establish an unlawful conspiracy under the statutes before us." 150 F. 2d at 745.

\(^{124}\) 316 U. S. 265 (1942).

competition. However, unfair methods of competition under Section 5 of the Federal Trade Commission Act\textsuperscript{136} include restraints of trade under the Sherman Act,\textsuperscript{137} and the order is based on a finding that the cement producers restrained price competition by agreement to employ the basing point system. The Circuit Court of Appeals for the Seventh Circuit, one judge dissenting, set aside the FTC order for lack of evidence of an agreement or conspiracy. Its opinion ascribed the uniformity of prices among producers to the necessity of meeting competitors' prices, and asserted that "there is no basis for the Commission's contention that the uniformity of delivered price was any evidence of collusion between the sellers..."\textsuperscript{138}

Price uniformity is not and should not be conclusive evidence of collusion or conspiracy. In economics, uniformity of prices in a single market at a moment of time is equally characteristic of pure competition, pure monopoly, monopolistic competition, and collusive agreement among sellers.\textsuperscript{139} But where neither the conditions of pure competition nor of pure monopoly are present, as in the tobacco industry, uniformity and stability of prices, combined with similarity of other practices and policies, signify to the economist the existence of monopolistic competition and to the lawyer evidence from which a conspiracy among the few powerful producers to suppress competition may be inferred.

A second feature of significance to the enforcing agencies is the relation of the American Tobacco decision to the problem of price leadership. Price leadership as an industrial phenomenon exists where as a result of custom or the dominance of one competitor the price and other policies of a particular company are voluntarily followed by all the other producers, without any agreement but simply because it appears to be good business on their part. Since all producers adapt their prices to those of the generally recognized leader, the leader exercises control similar to that in a group agreement, prices move together and the price set is the monopoly one.\textsuperscript{140} While price leadership may be found in a

\textsuperscript{136} 38 \textit{STAT.} 719 (1914), as amended, 15 U. S. C. §45 (1940).
\textsuperscript{139} \textit{HANDLER, A STUDY OF THE CONSTRUCTION AND ENFORCEMENT OF THE FEDERAL ANTITRUST LAWS} 35 (TNEC Monograph 38, 1941).
\textsuperscript{140} \textit{BURNS, THE DECLINE OF COMPETITION} cc. 3, 5 (1936); \textit{CHAMBERLIN, THE THEORY OF MONOPOLISTIC COMPETITION} 50 n. 1 (5th ed. 1946); \textit{Comer, PRICE LEADERSHIP, 7 LAW & CONTEMP. PROB.} 61 (1940); Note, 29 CALIF. L. REV. 507 (1941).
market of many sellers, it is more easily maintained and more common where sellers are few and one of their number is dominant. Although price competition is clearly eliminated, price leadership has been held not a violation of the Sherman Act because the essential element of agreement could not be proved.\textsuperscript{141}

There is no recognized price leader in the tobacco industry, although Reynolds has initiated more changes than any other company,\textsuperscript{142} and price leadership was not involved or mentioned in the case. Yet the inference of conspiracy drawn from identity of prices and practices may yet circumvent the obstacle to antitrust action in price leadership situations. The government can argue that uniformity of prices and the custom of following the price leader flow from an understanding and agreement among all producers to fix prices by tying them to the price movements of the leader. Strong support for this approach is found in Justice Douglas' language in the Masonite case:\textsuperscript{143}

"Nor can the fact that Masonite alone fixed the prices and that the other appellees never consulted with Masonite concerning them make the combination any the less illegal. Prices are fixed when they are agreed upon. . . . The fixing of prices by one member of a group pursuant to express delegation, acquiescence, or understanding is just as illegal as the fixing of prices by direct, joint action."\textsuperscript{144}

The American Tobacco case's third contribution to antitrust law enforcement is its expansion of the concept of "monopolization" under Section 2 of the Act. Although loose combinations and conspiracies have previously been held violations of Section 2 as well as Section 1,\textsuperscript{145} the monopoly section has been confined largely to mergers, holding


\textsuperscript{142}Of eleven changes since 1928, two were caused by tax increases, one was granted by OPA at the request of all manufacturers, Reynolds initiated five and American three. Cox, \textit{Competition in the American Tobacco Industry} 187-218 (1933); \textit{Ann. Rep. on Tobacco Statistics} (1937-46); \textit{Standard & Poor's Industry Survey: Tobacco}, Part II, T4-3, April 10, 1946; Tobacco, Oct. 10, 1946, p. 3.

\textsuperscript{143}Id. at 275-6.

\textsuperscript{144}Id. at 316 U. S. 265 (1942).

\textsuperscript{145}Associated Press v. United States, 326 U. S. 1 (1945) (members of ass'n agreed not to sell news to non-members and granted each member power to block competitors from membership); Hartford-Empire Co. v. United States, 323 U. S. 386 (1945), 324 U. S. 570 (1945) (manufacturers of glass-making machinery and glass products through patents and agreements monopolized the industry); United States v. Crescent Amusement Co., 323 U. S. 173 (1944) (combination of motion picture exhibitors used buying power to coerce distributors and exclude competing exhibitors); United States v. Masonite Corp., 316 U. S. 265 (1942) (price-fixing combination among manufacturers and distributors of building materials); United States v. Swift & Co., 286 U. S. 106 (1932) (consent decree involving monopolistic
companies and integrated industrial combinations. This decision demonstrates how effectively evidence of conspiracy among leading producers to fix prices and eliminate competition may be used to prove conspiracy to monopolize and group monopolization of an industry. Every conspiracy in restraint of trade is not a conspiracy to monopolize nor a monopolization, but where the conspiracy involves the largest companies in an industry and a high combined percentage of total production, monopoly power is not difficult to prove. Thus, subject to as yet undefined limitations on multiple punishment, actions may be brought under both Sections 1 and 2 against the dominant corporations in an industry characterized by a few big producers, differentiated products and identity of business conduct.

In its authoritative holding that exercise of power to exclude or exclusion of competitors is not essential to monopolization, the Supreme Court lightened the Government's burden in antitrust litigation and


147 "The crime defined by Section 1 is legally distinct from the crime defined by Section 2. Offenses under these sections are not identical even though all the evidence is applicable to a count under Section 1, as well as to a count under Section 2." American Tobacco Co. v. United States, 147 F. 2d at 117. In United States v. Socony-Vacuum Oil Co., 310 U. S. 150, 226 n. 59 (1940), Justice Douglas states that the two sections overlap in that a monopoly under §2 is a species of restraint of trade under §1. His distinguishing element is the "existence or exertion of power to accomplish the desired objective." Thus a conspiracy to fix prices may be an illegal restraint of trade though the parties lack power to fix prices. Ibid. Judge Hand in United States v. Aluminum Co. of America, 148 F. 2d 416 (1945) expressed the distinction as follows: "Starting, however, with the authoritative premise that all contracts fixing prices are unconditionally prohibited, the only possible difference between them and a monopoly is that while a monopoly necessarily involves an equal, or even greater, power to fix prices, its mere existence might be thought not to constitute an exercise of that power. That distinction is nevertheless purely formal; . . . it would disappear as soon as the monopoly began to operate; . . . Indeed it would be absurd to condemn such contracts unconditionally, and not to extend the condemnation to monopolies; for the contracts are only steps toward that entire control which monopoly confers: they are really partial monopolies." Id. at 427-8. Thus the additional factor which makes a restraint of trade a monopoly is the existence of power to exclude competitors, i.e., power to control the market or the industry.

148 Defendants argued strenuously that their conviction under counts of conspiracy in restraint of trade, monopolization and conspiracy to monopolize subjected them to multiple punishment for the same offense, contrary to the Fifth Amendment. Brief for Appellant American Tobacco Co., pp. 138-59; Brief for Appellant Liggett & Myers Tobacco Co., p. 80; Brief for Appellant R. J. Reynolds Tobacco Co., pp. 93-100. Justice Rutledge, in his concurring opinion, expressly reserves judgment on this issue, which was not squarely within the limited certiorari granted by the Court. American Tobacco Co. v. United States, 328 U. S. at 815-6.

brought the legal concept of monopoly into closer harmony with the economic concept.\textsuperscript{150} In conjunction with the opinion of the Circuit Court of Appeals for the Second Circuit in \textit{United States v. Aluminum Co. of America},\textsuperscript{151} from which it quoted with approval,\textsuperscript{152} the \textit{American Tobacco} case establishes the elements of an unlawful monopoly. The monopoly may be a single company like the Aluminum Company, or a combination and conspiracy of the leading companies in an industry, like the tobacco companies. It must have power to exclude actual or potential competitors and must intend to exercise that power.\textsuperscript{153} The latter requirement is not of any "specific" intent, but only an intention to conduct business operations along lines which may appear normal and rational to businessmen but which have the effect of maintaining the monopoly's hold on the market.\textsuperscript{154}

The most obvious way to prove power to exclude is by evidence of exclusion of actual competitors, driving them out of the market with predatory practices, etc. Slightly more difficult is proof of exclusion of potential competition by buying up new companies, natural resources, raw materials, patents or trade marks, or perhaps by conducting large scale advertising campaigns. That such action, even when considered good business policy, may lay a company or combination open to a charge of monopolizing is indicated by Judge Learned Hand's reply to the Aluminum Company:

"It insists that it never excluded competitors; but we can think of no more effective exclusion than progressively to embrace each new opportunity as it opened, and to face every newcomer with new capacity already geared into a great organization, having the advantage of experience, trade connections and the elite of personnel. Only in case we interpret 'exclusion' as limited to manoeuvres not honestly industrial, but actuated solely by a desire to

\textsuperscript{150} See Mason, \textit{Monopoly in Law and Economics}, 47 \textit{Yale L. J.} 34 (1937). The author states that the legal concept of monopoly has been restraint of competition, in both loose and integrated combination cases, and the economic concept has been control of the market.

\textsuperscript{151} 148 F. 2d 416 (C. C. A. 2d 1945). This was a suit in equity brought under §§1 and 2 of the Sherman Act to adjudge that defendant company was monopolizing the aluminum ingot market and to dissolve it. The Circuit Court of Appeals for the Second Circuit sat as the final appellate court under a statute authorizing it to render a decision in lieu of a decision by the Supreme Court, where a quorum of qualified justices could not be had in that Court. 32 Stat. 823 (1903), 15 U. S. C. §29 (1940), as amended, 58 Stat. 272 (1944), 15 U. S. C. §29 (Supp. 1946).

\textsuperscript{152} American Tobacco Co. v. United States, 328 U. S. at 813-4.

\textsuperscript{153} Id. at 809.

\textsuperscript{154} Judge Learned Hand summarized the element of intent as follows: "In order to fall within §2, the monopolist must have the power to monopolize and the intent to monopolize. To read the passage as demanding any 'specific' intent, makes nonsense of it, for no monopolist monopolizes unconscious of what he is doing." United States v. Aluminum Co. of America, 148 F. 2d 416, 432 (C. C. A. 2d 1945), quoted in American Tobacco Co. v. United States, 328 U. S. at 814.
prevent competition, can such a course, indefatigably pursued, be deemed not "exclusionary." 155

In the final analysis, power to exclude competitors is simply another term for power to control the market, which is a practical economic description of monopoly: 156 "... monopoly may be said to exist whenever a single seller or a number of sellers acting in unison control enough of the supply of a broadly defined commodity to enable them to augment their profit by limiting output and raising price." 157 Control of the market may be evidenced by a combination's proportion of total production or sales, behavior of prices and output, relation of prices and costs, profits before and after the combination, presence of business practices such as price discrimination, price stability and others, and existence of potential competition. 158 The complexity of the legal standard, the necessity of weighing different factors, and the diversity of industrial situations undoubtedly mean that in the future, as in the past, each case will be a decision on its own individual facts, of limited applicability as a precedent.

One qualification must be added. The fact that a company or combination has monopoly power, power to control the market and exclude competitors, is not alone sufficient to condemn it. Use of the active verb "monopolize" in the statute leaves open an avenue of escape for the combination which can show that it has a natural monopoly, that it did not achieve or acquire monopoly but had monopoly "thrust upon it." 159 However, this loophole is likely to prove too narrow for frequent use. 160

The tobacco companies. To the tobacco manufacturers the decision seems to convict them for conspiracy when they have not conspired, to condemn their past activities without furnishing a guide for future conduct. With one voice they ask what they must do to avoid future prosecution under the Sherman Act. 161 If the defendants actually

156 Mason, supra note 150, at 41-2.
157 Wilcox, Competition and Monopoly in American Industry 10 (TNEC Monograph 21, 1940).
160 Judge Hand gives three abstract examples of monopoly "by force of accident": (1) A market may be so limited that it is impossible to produce at all and meet the cost of production except by a plant large enough to supply the whole demand. (2) Changes in taste or in cost may drive out all but one producer. (3) A single producer may be the survivor out of a group of active competitors, merely by virtue of his superior skill, foresight and industry. Id. at 430.
161 Petition for Certiorari of Appellant Liggett & Myers Tobacco Co., p. 5; Petition for Certiorari of Appellant R. J. Reynolds Tobacco Co., pp. 12-13; Reply Brief of Appellant American Tobacco Co., pp. 6-7. According to Liggett at the argument in the circuit court of appeals Government counsel was asked how an
engaged in a conspiracy or agreement, express or tacit, the simple answer is abandonment of the conspiracy. But if the basic practices and policies of the companies which convicted them were the natural features of business conduct in a monopolistic competitive industry, the answer is not so obvious. Perhaps by merely operating their businesses under these conditions the companies are contravening the policy of the Act and creating evidence of new violations.

Of course, the Big Three can learn from past mistakes. They probably will not hike the price of cigarettes at the bottom of the next depression. If cheaper cigarettes are demanded they can produce new economy brands of their own rather than lose sales to competing manufacturers. If control of distributors' prices seems desirable this may be accomplished legally in the forty-five states which have resale price maintenance statutes. Buyers, supervisors and salesmen may be carefully instructed to shun practices which create an impression of collusion. Slight departures from identical factory prices, such as Reynolds 1946 move, may have some small value as evidence for the defendants in another antitrust case.

But all these precautions will not change the fundamental similarity or identity of conduct among the major producers. For American, Reynolds and Liggett the only real answer is a frank recognition that the tobacco industry is not automatically regulated in the public interest by the Unseen Hand of classic competition, that within broad limits the policies made and administered by each company determine for the industry prices, production, wages, nature of product, use of resources, and relation to the economy as a whole. It follows that these policies must taken into consideration the interests of farmers, laborers, storekeepers and consumers, as well as the interests of the corporations and their stockholders. And, ironically enough, if one of the Big Three adopts farsighted and beneficent policies the very conditions which led to identical monopolistic practices will force the others to follow the new and wiser lead. Such a course of action might not constitute a legal defense under antitrust law but as a practical matter it would render the industry virtually immune to prosecution.

The public. The final decision in the tobacco case must raise in the public mind many more questions than it settles, questions of vital, practical import. Must the tobacco industry be prosecuted periodically for Sherman Act violations? Did the 1911 decree fail to establish com-
petition? Will the 1946 case restore competition and prevent monopoly? Are heavier fines or jail sentences the answer? Can competition be restored to the industry? If so, how? Is competition as the principle regulating force in this and other industries desirable? Should a larger measure of government control be introduced? If so, what kind and what degree of control?

The answers to some of these searching inquiries are fairly clear; others evoke differences of opinion which time alone will resolve. From his study of the industry in 1932 Cox concluded that the 1911 decree failed to produce anything more than non-price competition (advertising, etc.) among the few large manufacturers. The benefits to society from this type of competition, whatever they may be, are not the economic consequences promised by competition in the traditional sense. If the dissolution decree of 1911 did not revive competition surely one would be rash to predict greater success for the recent conviction and punishment of the Big Three. Events from 1940 to 1947 confirm expectations based on economic analysis—there has been no real change in the industry, competition still means rivalry in publicity and promotion, concentration and monopoly power have not been broken. Nor would heavier fines or jailing individual defendants have re-created competition in the industry as long as basic conditions remained unchanged.

Faced with this problem, the failure of antitrust action alone to preserve competition, the public must decide, consciously or unconsciously, on a future policy toward this and similar segments of the economy. Three main roads are open. The first is to accept conditions as they are, to depend on non-price competition, the presence of substitutes, the existing elasticity of demand, the possibility of new competition, the fear of antitrust prosecution and the wisdom and restraint of business leaders to protect the public from the evils of monopoly. This policy is a "free enterprise" approach if that term means freedom from further governmental regulation or interference. It avoids the difficulties and uncertainties of attempting to restore effective competition or to devise a workable substitute. The industry if left alone would probably continue to produce large quantities and varieties of tobacco products, to use efficient methods of machine production, to maintain stable selling prices, profits and dividends, and to contribute financial

163 Cox, Competition in the American Tobacco Industry 316-24 (1933).

164 The Department of Justice admits this. "For example, criminal action against the three largest cigarette manufacturers . . . resulted in fines of $255,000. . . . It is doubtful that this criminal action will change the high degree of concentration already existing in the industry and affect the preponderant economic power enjoyed by them. The Justice Department in its answer recognizes this and indicates that it is presently considering the advisability of taking civil action." Staff Report of the Monopoly Subcommittee, supra note 149, at 35.
support to newspapers, magazines, radio broadcasting and other advertising media.

But there are decided disadvantages inherent in such a course. The factors which are relied on to protect consumers, distributors, small competitors, workers and farmers from injury have not protected them in the past and can hardly be expected to do so in the future. One fact about the industry is highly significant. Production and consumption of cigarettes, the leading product, has been steadily expanding for over thirty years. This long-run growth of total demand has unquestionably had a salutary influence in the determination of industrial policy by the Big Three. With annually expanding sales volume maximum profits may be obtained at prices lower than the static monopoly price. But it is almost inevitable that some day the rise in per capita consumption will cease and production will either increase slowly, remain constant or even decline. When this happens an important restraint on the industry's monopolistic tendencies will have been removed and the policies and practices of the major companies may become intolerable.165

Without effective competitive pressure, high prices, inferior quality, inefficiency, excess productive capacity and resistance to economic change are likely to characterize the industry. As Judge Hand puts it in the Aluminum case:

"Indeed, even though we disregard all but economic considerations, it would by no means follow that such concentration of producing power is to be desired, when it has not been used extortiously. Many people believe that possession of unchallenged economic power deadens initiative, discourages thrift and depresses energy; that immunity from competition is a narcotic, and rivalry is a stimulant, to industrial progress; that the spur of constant stress is necessary to counteract an inevitable disposition to let well enough alone."166

In addition to economic, there are also social and political objections to such concentrations of economic power as exist in the tobacco and other major manufacturing industries. They contribute to inequality of income distribution, accentuate the separation of corporate ownership and control, reduce individual initiative and independence, weaken the system of free private enterprise, lead to demands for more governmental supervision and control, and beget a concentration of power in the state which endangers representative democracy.

A second approach to the problem adopts the traditional policy of antitrust law—restoration and maintenance of competition as the prin-

165 Cox, supra note 163, at 320-1.
ciple regulator of industry. There are, of course, some areas of the economy which are less conducive to competition than others, but manufacture of tobacco products is not one of them. No natural resources would be wasted by competition in this industry. No public utility function demands unified control and development. No technological factors of production necessitate plants or enterprises as large as American, Liggett or Reynolds. Workable competition can be restored to the industry, but not by half-hearted attempts to achieve a painless solution. Concentration and monopoly must be broken and loosening their grip is always painful.

A positive program to revive competition must have for its goal the creation of conditions essential to competition—a large number of independent sellers, standardized or readily substituted products, and the threats of potential competition. Two methods of establishing a sufficient number of independent sellers suggest themselves. One is dissolution of the seven defendant manufacturing corporations into many small companies, plus continuing efforts to maintain easy ingress into the industry. The other is to leave the present firms intact but actively retard their operations and stimulate the formation and growth of new enterprises. Either course would require vigorous antitrust law enforcement to prevent collusive agreement or coercive suppression of new competition. And vigorous enforcement will continue to be impossible until adequate staffs and funds are provided the Antitrust Division of the Department of Justice and the Federal Trade Commission.

Dissolution of the tobacco corporations could not be ordered in an antitrust suit under present law because the violation charged would be conspiracy and combination of independent firms; destruction of the separate entities would not appear logically or legally necessary to

267 See Wilcox, supra note 157, at 14-16.
268 See supra note 157, at 14-16.
269 "It seems necessary to conclude that in the tobacco industry while the large factory has a decided advantage over the small, there is a very broad range of sizes within which plants are approximately comparable in economic efficiency." Cox, supra note 163, at 111. Cox points out that the advantages in large enterprises (as distinct from large plants) are in financial administration and sales promotion rather than in technology. Id. at 112-5.
270 Workable or effective competition among sellers is not necessarily pure or perfect competition but is a condition which offers buyers real alternatives sufficient to enable them, by shifting their purchases from one seller to another, substantially to influence quality, service, and price. Wilcox, supra note 157, at 8-9.
271 Two instances illustrate the disparity between federal appropriations and the magnitude of the job. In the recent cement industry case three FTC attorneys opposed lawyers from forty-one law firms, and defendant companies spent over $5,000,000 on the case, or about twice the annual FTC appropriation. Staff Report of the Monopoly Subcommittee, supra note 149, at 29. In Hartford-Empire Co. v. United States, 323 U. S. 386 (1945) defendants spent an estimated $2,000,000, or considerably more than the average annual appropriation for the whole Antitrust Division; five attorneys for the Division opposed thirty for the defense. Id. at 47.
destroy the conspiracy and combination. The new legislation needed might prescribe corporate dissolution as a penalty for antitrust violation, the details to be worked out by an administrative agency. Or it might take the form of a federal incorporation law limiting the size and power of corporations in interstate commerce, with gradual dissolution of firms which exceeded the permissible limits. One of the thorniest aspects of dissolution in the tobacco industry would be disposition of trade-marks and brand names; perhaps use of present brand names by any of the newly created corporations would be the only practical solution.

If not dissolved, the major companies would have to be held back, not only by watchful antitrust supervision, but also by positive measures to give small manufacturers a competitive advantage. To secure a proportional tax burden for the cheaper cigarettes the federal cigarette tax should be graduated according to the retail prices of the brands, like the rates on cigars. To reduce the burden of large capital investment in leaf tobacco inventory and to bolster the farmers’ bargaining power government owned or financed redrying and storage warehouses should be established for the use of growers, buyers and manufacturers. To prevent elimination of firms by consolidations or mergers the Federal Trade Commission should be given authority to forbid acquisition of the stock or assets of competing corporations unless such action is in the public interest and will not lessen competition.

On the general problem of dissolution see Hale, Trust Dissolution: "Atom-izing" Business Units of Monopolistic Size, 40 Col. L. Rev. 615 (1940).

Large cigars are divided into seven tax rate classes, according to their retail prices, which vary from 2½ cents each or less in Class A to more than 20 cents each in Class G, whereas all small cigarettes are taxed at the same rate per thousand. Ann. Rep. on Tobacco Statistics 50 (U. S. Dep't Agric. 1946). This means that buyers of "economy" cigarettes are paying a proportionately larger amount in taxes than smokers of the "popular" brands. The Federal Trade Commission has recommended a graduated cigarette tax as an aid to competition. Hearings before the Temporary National Economic Committee, Part 5A, 76th Cong., 1st Sess. 2392 (1939).

Section 7 of the Clayton Act, 38 Stat. 731 (1914), 15 U. S. C. §18 (1940), prohibits a corporation’s acquisition of part or all of the stock of another corporation where the effect may be to substantially lessen competition between them, or to restrain commerce, or tend to create a monopoly. The obvious weakness of the statute, its failure to prohibit acquisition of assets of another corporation, was compounded by Supreme Court decisions holding that the Federal Trade Commission could not order divestiture of assets obtained by unlawful stock purchases, even where such assets were transferred after the commencement of FTC proceedings for divestiture of the stock. Arrow-Hart & Hegeman Electric Co. v. Federal Trade Comm’n, 291 U. S. 587 (1934); Federal Trade Comm’n v. Western Meat Co., 272 U. S. 554 (1926). Since these decisions the merger process has gone merrily on, and the high degree of concentration in many industries today is largely attributable to mergers and consolidations among competitors. The tragic futility of attempting through antitrust litigation to dissolve combinations which should have been caught in their inception has led to repeated recommendations for legislative reform. See President Truman’s Economic Report to Congress, N. Y. Times, Jan. 9, 1947, p. 15, col. 1; Temporary National Economic Committee, Final Report and Recommendations, Sen. Doc. No. 35, 77th Cong,
Measures short of dissolution would have to reckon with the differentiation of product and extensive brand advertising of the leading companies. Grade labeling of tobacco products under government inspection and standards would enable consumers to distinguish between quality of product and superior sales promotion. Legislation providing for forfeiture of trade marks and trade names upon proof of their use in antitrust violations would be constructive. But new brand names can be publicized and promoted, and as long as huge advertising campaigns are essential to sales volume new firms will not enter the industry and potential competition will not effectively limit monopoly power. A way must be found to restrict sales promotion or confine it to class of commodity rather than particular brand (i.e., cigarettes generally rather than Luckies or Camels). Restriction of this protective device of monopoly offers the only hope for the evolution of a tobacco industry of many producers and effective competition.

If the public decides that some action is necessary but workable competition cannot be revived in the industry, a third course is available—determination of industrial policy by a governmental agency. Wartime experience with price control proves that this is entirely feasible and can produce desired results.

On December 27, 1941, American announced a price increase on Lucky Strike cigarettes, and upon refusal of the company to rescind the increase voluntarily pending investigation, the Price Administrator, acting under executive authority (later superseded by the Emergency Price Control Act of 1942), froze all manufacturers' cigarette prices at levels prevailing on December 26, 1941. No change in the net price of Luckies, Camels, Chesterfields and other popular or standard brands was permitted from that date until April, 1946, but an increase
in maximum prices of economy cigarettes was granted by the Office of Price Administration in September, 1943. On April 25, 1946, in response to appeals based on higher manufacturing costs, the Price Administrator raised the ceiling price of the popular brands 25 cents per thousand. And in October of the same year, after price controls had been removed, the companies, led by American, added another 25 cents per thousand to their net cigarette prices.

During the four years in which net manufacturers' prices on popular brands remained unchanged cigarette production rose 52%, per capita consumption 47%. Average prices of flue-cured tobacco increased 56%, burley tobacco 35% and Maryland tobacco 89%, but the steady upward trend of production enabled cigarette manufacturers to absorb these increases in raw material costs without a rise in product prices. However, with stationary cigarette prices and advancing costs the expansion of sales volume could not prevent a substantial effect on profits. From 1941 to 1945 American, Reynolds, Liggett, Philip Morris and Lorillard increased not only their production of cigarettes but also their share of the total market, but profits dropped both absolutely and relatively. These firms' ratio of net income (after taxes) to net worth averaged 12.23% in 1941, 11.46% in 1942, 9.92% in 1943, 8.98% in 1944 and 8.85% in 1945. In 1946, the year in which two price rises occurred, profits started upward again with a figure of 10.25% of net worth. This first post-war year

\begin{table}
\begin{tabular}{|c|c|c|c|}
\hline
Year & Flue-cured & Burley & Maryland \\
\hline
1936-39 & 20.6 & 23.0 & 20.5 \\
1941 & 28.1 & 29.2 & 30.1 \\
1942 & 38.4 & 41.8 & 56.5 \\
1943 & 40.2 & 45.6 & 45.3 \\
1944 & 42.4 & 44.0 & 55.5 \\
1945 & 43.7 & 39.4 & 56.8 \\
\hline
\end{tabular}
\end{table}

\textsuperscript{177} OPA Revised Price Schedule No. 62—Cigarettes, Amendment 2, 9 Fed. Reg. 2667 (1944). The list price ceiling was raised from $5.15 to $5.82 a thousand.


\textsuperscript{179} Tobacco, Oct. 10, 1946, p. 3, Oct. 17, 1946, p. 3.

\textsuperscript{180} ANN. REP. ON TOBACCO STATISTICS 46 (U. S. Dep't Agric. 1946). The 1941 figure was 217.9 billion cigarettes; the 1945 total was 332.2 billion.

\textsuperscript{181} Id. at 47. Per capita consumption was 1,580 in 1941 and 2,330 in 1945; figures for both years include U. S. armed forces overseas.

\textsuperscript{182} Id. at 15-16. A comparison of average leaf tobacco prices (in cents per pound) for the base period 1936-39 and the years of cigarette price control follows:


\textsuperscript{184} The leading brands of these five companies increased their share of total domestic production from 72% to 84% during the period. STANDARD & POOR'S INDUSTRY SURVEY: TOBACCO, Part II, T4-5, April 10, 1946.

\textsuperscript{185} Combined net income, before taxes and reserves, for the five companies was $133,000,000 in 1941 and $127,000,000 in 1945. MOODY'S INDUSTRIALS 1957, 1970, 2439, 2480, 2684 (1946), and prior years.

\textsuperscript{186} Ibid.

\textsuperscript{187} MOODY'S INDUSTRIALS (Manual Service 1947).
also saw a renewal of the huge advertising expenditures which had been severely cut during the war.\textsuperscript{188}

This record of the tobacco industry under price control demonstrates that cigarette prices can be effectively regulated in the public interest without curbing production or precluding non-price competition and reasonable profits for producers. Nor does price control at the manufacturers’ level necessarily imply control of distributors’ prices; competition among the thousands of wholesale and retail outlets can be relied on to keep prices at reasonable figures. Minimum prices might have to be established for leaf tobacco, however, if the present federal government quota system\textsuperscript{189} does not protect the tobacco farmers against depressed prices caused by the small number of buyers in the auction markets.

Whichever public policy is adopted, whether reliance on existing conditions, action to restore effective competition or regulation by an administrative agency, the decision should be based on thorough investigation and full information on all phases of the tobacco business. If it achieves no other tangible and immediate goal, the recent antitrust prosecution of the major companies has disclosed the basic facts of industry operations over the past thirty years, facts which are essential for any satisfactory answer to the serious questions raised by the final judicial decision.

\textbf{Conclusion}

In the \textit{American Tobacco Company} case the Government won a legal victory. It convicted the leading tobacco companies of antitrust violations. It applied the Sherman Act to the most prevalent form of monopoly in American industry and sharpened that Act’s potentialities for the future. But the Government did not win an economic victory, and therein lies the fundamental weakness of our traditional antitrust policy. If the persistent incursions of monopoly into the narrowing area of free competitive enterprise are to be halted, effective sanctions must be devel-

\textsuperscript{188} N. Y. Times, Mar. 11, 1946, p. 32, Mar. 29, 1946, p. 29, April 26, 1946, p. 37.

\textsuperscript{189} The Agricultural Adjustment Act of 1938, 52 STAT. 31 (1938), as amended, 7 U. S. C. §§1281 \textit{et seq}. (1940), imposes national, state and farm marketing quotas for leaf tobacco when the Secretary of Agriculture finds that the total supply at the beginning of the marketing year exceeds the “reserve supply level” as defined in the Act, and when two-thirds of the tobacco farmers voting at a referendum approve the imposition of quotas. The Act was held constitutional in \textit{Mulford v. Smith}, 307 U. S. 38 (1939). Another federal statute regulating tobacco marketing in the interest of the growers is the Tobacco Inspection Act, 49 STAT. 731 (1935), 7 U. S. C. §§511-514q (1940), which provides for government inspection and grading of leaf tobacco at designated auction markets, in order to standardize grades and furnish farmers with information necessary for intelligent market decisions. This Act was held constitutional in \textit{Currin v. Wallace}, 306 U. S. 1 (1939).
oped and applied to industries which are judicially declared monopolis-
tic. New federal legislation authorizing legal and economic measures
to revive competition and to maintain conditions essential for competition
in such industries seems imperative. The alternative is abandonment of
competition and increasing reliance on state control and direction of the
economy in order to achieve the maximum economic benefits of a modern
scientific and industrial society.