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The Northern Securities Decision

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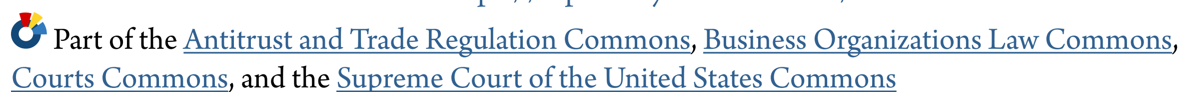
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THE NORTHERN SECURITIES DECISION

MARCH 14 the Supreme Court of the United States decided one of the most important cases that has been before it for a number of years. The litigation referred to is the Northern Securities case. The question involved was whether the control of the Great Northern and Northern Pacific railway companies through the ownership of the majority of the stock of each of those companies by the Securities company violated the national anti-trust act. The majority of the Supreme Court held it did, but four of the judges dissented.

A short history of the matter is necessary to understand the decision. The Northern Pacific Company was chartered in 1864 and after passing through two receiverships came largely under the control of Mr. J. P. Morgan and his associates. It received from the government an extensive land grant, nearly equal in area to the states of Indiana and Ohio, and in the national charter granted to it it was provided that the government might at any time alter, amend, or repeal the same. When it was reorganized the second time, it was incorporated under the laws of Wisconsin. The Great Northern Company is incorporated in Minnesota and leases for 999 years various lines of railway most of which were constructed by the St. Paul, Minneapolis, and Manitoba company. This latter company was the successor of the old St. Paul and Pacific company which went into the hands of a receiver in 1873, and was reorganized in 1879 under proceedings foreclosing a mortgage, the purchase of the road having been made by Mr. James J. Hill and his associates. The line was completed to the Pacific coast about 1889, and it then became a competitor of the Northern Pacific road. These two roads extend from Duluth, through St. Paul, on west, through Spokane, to the Pacific coast. Their lines are substantially parallel throughout their whole extent, and if operated independently would be competitors throughout nearly the whole field.

For a number of years there have been attempts to bring the operation of these two lines into harmony. When the Northern Pacific was in the hands of a receiver the last time, a plan of reorganization was proposed which provided that one hundred million dollars of bonds should be issued by a new Northern Pacific Company to take up all of the bonds of the old company, and that the capital stock of the new company should be one hundred million dollars. The Great Northern Company proposed to guarantee the bonds of the Northern Pacific if it might be allowed to become the owner of half the capital stock of the new company. A shareholder in the Northern Pacific Company objected to this and brought suit to prevent the consummation of the plan. This suit was taken to the Supreme Court of the United States, where it was held that the proposed plan violated the Minnesota law forbidding the consolidation of parallel and competing lines of railway. The opinion in this case was delivered by Mr. Justice Brown, a present member of the Supreme Court, who held that the ownership of half of the capital stock of the Northern Pacific road by the Great Northern was substantially a consolidation of the two lines. This plan was then abandoned. Mr. Morgan knew of the plan and approved it, and after the decision of the court assured Mr. Hill that they might operate or continue to operate the two roads in harmony.

In order to make these assurances good a new scheme of reorganization was proposed. A charter of an old railroad company was resurrected in Wisconsin, which did not reserve to the state the right to repeal or amend

it. *Quo warranto* proceedings were brought to test its validity and a decision was obtained holding it to be valid. This charter was used for reorganization purposes and one hundred million dollars or over of bonds were to be issued to take up the existing bonds of the Northern Pacific Company. There were to be one hundred and fifty-five million dollars of capital stock, divided into eighty million common and seventy-five million preferred. A special provision of the common stock allowed the owners thereof, on the first of January after a certain year, to retire at par any or all of the preferred stock. A part of this reorganization scheme also provided that every shareholder and bondholder of the Northern Pacific company who wished a share in the reorganization proceedings should agree to leave or deposit his shares or bonds with J. P. Morgan & Co. as managers, and a voting trust was arranged whereby Mr. J. P. Morgan and two others were to have for five years the right to vote all of the shares of the Northern Pacific company.

In this way Mr. Morgan and Mr. Hill were enabled to operate the two roads in harmony for five years, at least. In the reorganization of the Northern Pacific company the old preferred shareholders paid to the company $16 in cash in addition to their old shares for an equal amount of preferred shares in the new company, and the common shareholders likewise paid $10 additional for the common shares of the new company. It was believed that the capital stock was worth no more in fact than the cash then paid in upon it. Within the next few years Mr. Hill and his associates became the purchasers of nearly twenty-six million dollars par value of the common stock of the Northern Pacific, it having cost them a little over four million. Four years later they were enabled to put it into the Northern Securities Company at the rate of $115 per share, a net profit of over twenty-five million dollars on their investment of four millions; and perhaps this profit fairly represents the value of operating the roads in harmony.

The voting trust would expire in 1901. Before this date it was deemed desirable for both of these roads, the Great Northern and the Northern Pacific, to have an outlet to Chicago. Mr. Morgan and Mr. Hill concluded that the Chicago, Burlington & Quincy R. R. was desirable for that purpose. They offered to purchase all of the outstanding stock of that company, nearly one hundred and eight million, at $200 per share, a price somewhat more than the market value of those shares. The two companies issued their joint bonds for the purpose of raising the money necessary to pay the two hundred and sixteen million for the stock of the Burlington company, and secured the same by deposit of the Burlington stock. The control of the Burlington road by these two companies in some measure interfered with or was likely to interfere with the eastern outlet from Omaha and Kansas City of the Union Pacific company. Through various consolidations and reorganizations of one kind and another for the past eight or ten years, the Union Pacific company had come into control of all the lines of the Pacific railways reaching from the Missouri river to the Pacific coast in the United States, except the Atchison, Topeka & Santa Fe, the Great Northern, and Northern Pacific. The northern line of the Union Pacific, extending from Omaha to Salt Lake City and on to Portland, Ore., was in a measure a parallel and competing line with the Northern Pacific. The Burlington lines reached from Chicago to Omaha, to Cheyenne, to Denver, and to Billings, Mont., as well as to St. Paul and many of these lines were parallel and competing with parts of the Union Pacific or Northern Pacific. Mr. E. H. Harriman as representative of the Union Pacific interests demanded that

he be allowed a share in the purchase of the Burlington system. This was refused. He immediately began the quiet purchase of shares of the Northern Pacific, and succeeded in acquiring thirty-seven million of the common stock, and forty-one million of the preferred, or seventy-eight million of both, which gave him in stockholders' meeting a clear majority of all the outstanding stock. Mr. Morgan then, as he said, became "apprehensive," and Mr. Hill later testified that had Mr. Harriman's plan not been foiled the Great Northern road would have been for sale. In order to checkmate Mr. Harriman, Mr. Hill and Mr. Morgan began purchasing the common shares of the Northern Pacific stock. The result was the panic upon the stock market in New York of May 9, 1901, when the price of common shares in Northern Pacific stock was forced up to one thousand dollars. Many persons were ruined, but Mr. Morgan and Mr. Hill had succeeded in purchasing fifteen million dollars worth of the common stock, which, with what they already had, gave them forty-one million or a clear majority of the common stock. They immediately notified Mr. Harriman that upon the first of the following January they would exercise their privilege of retiring the preferred stock at par. In this way they would be able to control the Northern Pacific.

A truce was, however, entered into between Mr. Harriman, and Mr. Hill and Mr. Morgan, whereby it was determined that the Northern Pacific directors should immediately resign and Mr. Morgan should appoint a directorate in which all the various interests involved should have fair representation. At the same time, (though, perhaps, contemplated for some time before,) it was agreed that there should be incorporated in New Jersey a new corporation with a capital stock of four hundred millions which should exchange its shares for the shares of the Great Northern and Northern Pacific companies in such manner that the shareholders of those two companies should afterwards become shareholders of the new company, and the new company should become substantially the sole shareholder in each of the other companies. This new company was named the Northern Securities Company, and by its articles of incorporation was to be exclusively a holding company and not apparently a railroad-operating company. For each one hundred dollar share of Northern Pacific stock there were to be issued $115 in the stock of the Northern Securities Company; and for each one hundred dollar share of Great Northern stock, there were to be issued $180 in the stock of the Northern Securities Company. At these prices the Securities stock was sufficient to take up very nearly all of the outstanding shares of the two companies. In this way the power to select the directors of the two companies became vested in the Securities company, and the shareholders of the two companies instead of being interested in the welfare and earnings of *each* company separately became interested in the welfare and earnings of *both* companies together. Thus all motive for operating them in any competitive way was gone.

The legality of the transaction was immediately questioned. Governor Van Sant of Minnesota called a meeting of the attorneys-general of the northwestern states to consider the matter, and they unanimously advised that suit be brought by one of the states to determine whether the combination formed did not violate the state anti-trust laws and the state laws forbidding the consolidation of parallel lines of railway. Minnesota immediately brought such a suit in the Supreme Court of the United States, but owing to a failure to name a necessary party as defendant and because there was not the requisite diversity of citizenship the Supreme Court held

it had not original jurisdiction. The state. however, thereupon brought suit in the state court. The case was removed at the instance of the defendant to the circuit court of the United States. In that court the decision of Judge Lochren was adverse to the state. The case was then appealed to the United States Supreme Court where it has been argued, but not decided. This case involves the extent of the power of the states over such combinations, and is as important or even more so, possibly, than the decision pronounced a few days ago. The state of Washington also brought suit in the Supreme Court of the United States. In this case the requisite parties were made defendants and the diversity of citizenship existed so that the Supreme Court has original jurisdiction. This case is now pending in the Supreme Court. The questions involved are substantially the same as those in the Minnesota case.

Very soon after the facts of the combination became known President Roosevelt asked Attorney-General Knox for his opinion as to the validity of the Securities company. He gave an opinion that in his judgment it violated the national anti-trust law, whereupon the President directed him to bring suit. The suit was promptly begun in the circuit court of the United States for the district of Minnesota. This case was heard before Judges Caldwell, Sanborn, Van Devanter, and Thayer. Judge Thayer pronounced the unanimous opinion of the court to the effect that the combination violated the national anti-trust act, and rendered a decree enjoining the shareholders of the companies from making any further transfer of shares, and the railroad companies from paying any dividends to the Securities company or allowing that company to vote for the election of directors of the railroad companies, and authorizing the Securities company to return the shares of the railroad companies to their former owners, and the shareholders in the Securities company to return their shares to that company.

The case was immediately taken to the Supreme Court of the United States. It was argued by Attorney-General Knox for the United States, by ex-Attorney-Geueral Griggs and by John G. Johnson, Esq., for the Securities company. The decision of the majority of the Supreme Court affirms the decision of the court below and approves the decree made in that case. Mr. Justice Harlan delivered an opinion in which concurred Justices Brown, McKenna, and Day. Mr. Justice Brewer delivered an opinion concurring in the result though not approving all that was said in the opinion of Justice Harlan. Mr. Chief Justice Fuller and Justices Peckham, Holmes, and White dissented. The last two delivered dissenting opinions.

The anti-trust act provides by the first section that every contract or combination in the form of trust or otherwise, or conspiracy in restraint of interstate or foreign trade or commerce shall be unlawful, and that every person who enters into such shall be guilty of a misdemeanor and punished by a fine not exceeding five thousand dollars or imprisonment not exceeding one year or both. Section two provides that any person who monopolizes or attempts to monopolize, or combines or conspires to monopolize such trade or commerce, shall be guilty and punished in the same way. The fourth section provides that upon suit by the attorney-general such combinations and parties thereto may be enjoined. The suit was brought under these provisions.

The first case under this act decided by the Supreme Court was the sugar trust case,—United States *v.* E. C. Knight Company.[1] Mr. Justice White in his dissenting opinion considers this

[1] 156 U. S. 1.

case to be "upon all fours" with the Securities case. Suit was brought in that case by the government to enjoin the carrying out of what the government alleged to be a monopoly in the production, manufacture, and sale of sugar by the American Sugar Refineries Company. This company, already in control of a large part of the sugar manufacturing, purchased the stock of four Philadelphia sugar refineries and thereby was enabled to control nearly 98 per cent of the sugar refining of the country. The government alleged that these contracts of purchase violated the anti-trust act, and undertook to establish its case by confining the evidence to the terms of these written contracts. Upon the face of the contracts there was insufficient evidence of any purpose to restrain competition or trade. This being the case the Supreme Court held that manufacturing things was not commerce, that the purchase of manufacturing plants was not commerce, that there was no evidence of any restraint of interstate commerce, and that whatever might have been the intention of parties purchasing such plants, the government had not made out a case within the anti-trust law. Mr. Justice Harlan alone dissented, and Mr. Justice Jackson took no part in the case.

The next two cases that came before the court were railroad cases involving the validity of agreements among railway companies fixing rates and dividing traffic. The first of these was the United States *v.* the Trans-Missouri Freight Association.[1] In this case the opinion of the majority of the court was delivered by Mr. Justice Peckham, who held that the anti-trust act applied to railroads, that it was not inconsistent with the interstate commerce law, that it applied to all contracts in restraint of trade and competition, and that it was not necessary for the government to show a purpose to restrain such trade if that was its necessary effect. Four judges dissented, Justices Field, Gray, White, and Shiras. Of these, only Justice White remains a member of the court. The next case was the United States *v.* the Joint Traffic Association, involving substantially the same question.[1] The opinion of the majority of the court was delivered by Mr. Justice Peckham. In this case the constitutionality of the law had been attacked, but the court held that the act was constitutional. Three judges, Gray, White, and Shiras, dissented in this case, Justice Field having retired, and Justice McKenna taking no part in the decision. The two cases that next came before the court involved the question whether persons who are members of a stock or merchants' exchange having certain rules and regulations providing that they would deal only with members of the association even though their purchases or sales might be made in different states, violated the anti-trust act. These cases were Hopkins *v.* the United States,[2] and Anderson *v.* United States.[3] The majority of the court held, by Mr. Justice Peckham, that the circumstances detailed above did not constitute a violation of the law. To both these decisions Mr. Justice Harlan dissented, but pronounced no opinion. The next case was the Addyston Pipe case.[4] This involved the question whether a combination of six companies engaged in manufacturing cast iron pipe, whereby through a committee consisting of one member from each company the price was fixed at which the companies would furnish pipe either to private purchasers or at public lettings, violated the anti-trust act. When a price had been fixed by this committee the various companies were asked to bid

[1] 166 U. S. 290.

[1] 171 U. S. 505.

[2] 171 U. S. 578.

[3] 171 U. S. 604.

[4] 171 U. S. 211.

THE SPANISH MORTAR—IN MEMORY OF THE UNIVERSITY MEN WHO FELL IN THE WAR WITH SPAIN

among themselves for the privilege of furnishing the pipe to the purchaser at such price. The company which offered the largest bonus for the privilege was to be awarded the contract, and the other companies in case of a public letting would bid a price higher than that agreed upon. The bonus was then to be divided among all the companies in proportion to their annual output. The companies controlled probably one-third of the production of cast iron pipe in the country and operated to a considerable extent throughout two thirds of the territory of the United States. The court by Mr. Justice Peckham pronounced an opinion against the Pipe Company, in which all of the judges concurred, the only case of this sort involving the trust act which has received the unanimous condemnation of the court.

Such had been the interpretation made by the court when the Securities case came before it. Mr. Justice Harlan very correctly announced that these cases had thus far determined that the anti-trust act embraces and declares to be illegal every contract, combination, or conspiracy in whatever form or whatever nature, and whoever may be parties to it, which directly or necessarily operates in restraint of trade or commerce among the several states or with foreign nations; that the act is not limited merely to unreasonable restraints of commerce, but is directed against all restraints, reasonable or unreasonable, imposed by any such combination; that railroads engaged in such commerce are embraced in the act; that companies, or even private manufacturers or dealers by whom such commerce is restrained are equally embraced by the act; that Congress has the power to establish rules by which such commerce shall be governed, and by the anti-trust act has prescribed the rule of free competition among those engaged in such commerce; that any combination which would extinguish competition between otherwise competing railroads engaged in such commerce is illegal; that the natural effect of competition is to increase commerce and an agreement the direct effect of which is to prevent this play of competition restrains instead of promotes such commerce; that to vitiate a combination condemned by the act it need not be shown that such combination in fact results or will result in total suppression of trade or in a complete monopoly, but it is only necessary to show that by its necessary operation it tends to restrain such commerce or to create a monopoly therein and to deprive the public of the advantage of free competition. The constitutional guaranty of liberty of contract does not prevent Congress from making the rule of free competition for those engaged in such commerce. These propositions seem to have been fully settled by the former decisions. But in the Northern Securities case the defendants claimed that their acts were simply acts of ownership of stock, and nothing more, and that therefore such acts were not interstate commerce and did not restrain such commerce. The government's contention was, first, that the acts of the shareholders of the Great Northern and Northern Pacific companies were such as to make in fact a combination among themselves whereby they were enabled to restrain competition between these two great interstate railroads, that their motive for further competition had been entirely removed, and that the natural tendency of this condition was and would be to prevent further competition between these two roads. And secondly, the government argued that even though the form of organization partook of the nature of ownership of shares, it nevertheless was a trust within the meaning of the act and was therefore illegal. Through the opinions of Mr. Justice Harlan and Mr. Justice Brewer the majority of the court decided that both these conten-

tions were correct. Upon the last point the decisions of the Supreme Court of Ohio in State *v.* Standard Oil Company,[1] and of New York in People *v.* North River Sugar Refinery Company,[2] and of Illinois in Distilling and Cattle Feeding Company *v.* People,[3] and Harding *v.* American Glucose Company,[4] ought to be conclusive as to what a trust is.

The dissenting opinion of Mr. Justice Holmes seems to have been based more upon what may be included in the words of the act, rather than what was actually accomplished or done and intended to be done by the parties in this particular case. He also considered the case as in a measure a penal suit, in which this statute must necessarily be strictly construed. Looking upon the transactions here as being very largely mere transfers of ownership of property rather than a combination of persons to restrain trade or commerce, and believing that the act was not designed to prevent one person in good faith from purchasing property, or to prevent a partnership from being formed which might purchase property and through such purchase incidentally cause the disappearance of all formerly existing competition, Mr. Justice Holmes therefore concluded that these acts should not be considered as being within the law. While these things suggested by Mr. Justice Holmes are undoubtedly puzzling in considering what is included within the meaning of the words, yet from the facts of this case as established by the evidence, it would seem that such discussion was in a measure academic if not entirely unnecessary. Somewhat the same criticism might be made upon the opinion of Mr. Justice White. He however expresses the view that if the majority opinion is correct, then the act so interpreted gives the national government a power to interfere with the regulation of the ownership of property within a state and therefore is unconstitutional as being in excess of the national authority. His fundamental proposition seems to be that the national government cannot regulate the ownership of property; and he deduces from that, another proposition to the effect that a power exists somewhere in the owners of property which gives them the right to use that property in such a way as to defeat the power of Congress to regulate interstate commerce and to annul an act designed therefor. His proposition seems to be exactly the reverse of that of the government and of the majority opinion. The government contended and the majority opinion seems to hold that no device by state, or corporation, or directors of corporations, or shareholders of corporations, or individuals shall be effectual to regulate interstate commerce contrary to an act of Congress designed to regulate the same, and that whatever property one may own he has no constitutional right to use it in a way that restrains interstate commerce contrary to the Congressional will. It is believed that the proposition contended for by the government and upheld by the majority opinion will be accepted as the correct one.

Mr. Justice Brown was ill when the case was argued, but was vouched in by consent of both parties, and upon the briefs submitted to him stood with the majority. While Mr. Justice Brewer did not concur in all particulars with Justice Harlan, yet his view can give no comfort to the Securities company. He held that the former decisions of the court had, perhaps, gone too far in holding that all contracts in restraint of trade, whether reasonable or unreasonable, were within the statute. Nevertheless he held that this combination was in unreasonable restraint of interstate commerce, and was therefore illegal.

[1] 49 Ohio State 137.
[2] 121 N. Y. 582.
[3] 156 Ill. 448.
[4] 182 Ill. 551.

It is believed that the decision of the majority is good law; that it is within the intention of the framers of the anti-trust act; that it is within the fair meaning of the words of that act; and that it is well within the rules laid down in former decisions. While, in some measure, it makes clearer the power of the government and the scope of the anti-trust act, it by no means settles all of the questions necessary to be settled before the evils of unrestricted combinations are done away with. The questions very naturally arise,—does the anti-trust act apply to the Burlington purchase? to the United States Steel Corporation? to the Western Union Telegraph Company? Whatever one may think upon these questions, they can only be answered at the end of long continued and hard fought litigation. If the newspaper reports are correct as to the new plan devised by the defendants in this case for returning the shares to the former shareholders, and if the president, the attorney-general, and the court are determined that their work shall not be annulled absolutely, the end of this case is not yet reached. Instead of returning to former Northern Pacific shareholders the shares they exchanged for Securities stock, the reported plan is to return to each of such $39.27 Northern Pacific, and $30.17 Great Northern stock; and the same method is to be applied to the return of the Great Northern shares. In this way the shareholders will become more completely than ever joint-owners and controllers of the two roads. It is believed that this violates both the anti-trust act and the decree rendered in the case. The defendants make such an interpretation of the decree at their peril, and, if we are not mistaken, may make themselves liable to contempt of court. What the government will do remains to be seen. The courts, in matters of this kind, must always be behind, instead of ahead of, the procession of law-breakers, for "trusty justice follows only after with slow and measured tread."

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