

Michigan Law Review

Volume 40 | Issue 2

1941

CONSUMERS' CO-OPERATIVES AND PRICE FIXING LAWS

Charles Bunn

University of Wisconsin Law School

Follow this and additional works at: <https://repository.law.umich.edu/mlr>



Part of the [Agriculture Law Commons](#), [Antitrust and Trade Regulation Commons](#), and the [Business Organizations Law Commons](#)

Recommended Citation

Charles Bunn, *CONSUMERS' CO-OPERATIVES AND PRICE FIXING LAWS*, 40 MICH. L. REV. 165 (1941).
Available at: <https://repository.law.umich.edu/mlr/vol40/iss2/2>

This Article is brought to you for free and open access by the Michigan Law Review at University of Michigan Law School Scholarship Repository. It has been accepted for inclusion in Michigan Law Review by an authorized editor of University of Michigan Law School Scholarship Repository. For more information, please contact mlaw.repository@umich.edu.

MICHIGAN LAW REVIEW

VOL. 40

DECEMBER, 1941

No. 2

CONSUMERS' CO-OPERATIVES AND PRICE FIXING LAWS

*Charles Bunn**

“THE evolution of our business institutions shows us a long procession of experimental procedures, giving rise to *de facto* commercial forms, many of which have in turn demanded such recognition *de jure* as should make their position in the business world both clear and safe.”¹ Consumers' co-operation is such a procedure. Its underlying idea is simple, that a business owned by its customers, managed under their direction and having no legitimate loyalties except to them, has a better chance to meet their needs than one owned and managed by outsiders. But it has taken many years and many failures to get this idea translated into practice, and to work out its appropriate legal form.

When a group of people organize to carry on a business they will no doubt create either a large partnership, or some kind of a corporation, or perhaps a business trust. Many co-operative societies have been organized informally, and are no doubt technically partnerships, but as in other businesses and for the same reasons the newer and the larger units are incorporated. They differ, however, from other business corporations in three chief respects:

1. *Patron ownership*: The shareholders or members of a co-operative association are chiefly the persons with or for whom it does business, not outside investors.

2. *Democratic government*: Voting power is by the rule “one vote per member,” not “one vote per share.”

3. *Patronage refund*: Dividends on capital either are not paid at all, or are paid at a fixed low rate. Remaining divisible net earnings are divided in proportion to business done with the association, not in proportion to shares held.

* Professor of Law, University of Wisconsin Law School, on leave 1941-1942. Acting Chief, Division of Exports and Defense Aid, U. S. State Department. A.B., Princeton; LL.B., Harvard; member, Minnesota bar. Author of articles in various law reviews.—*Ed.*

¹ NOURSE, THE LEGAL STATUS OF AGRICULTURAL CO-OPERATION 7 (1927).

None of these statements, except possibly the third, can be made as absolutely true of all co-operatives. But they are generally true, and they constitute the chief legal differences between co-operatives and other business corporations.²

It will be seen at once that the underlying notion is not new. Mutual insurance companies have followed co-operative principles for years (with reservations on the point of democratic government) and might well have been claimed by the co-operative movement as the most prominent and substantial exponents of its doctrines. There are indeed some insurance corporations which call themselves "co-operative," but the common word is "mutual," and they are not generally thought of in connection with the movement. Credit unions are so thought of, but their law is of course special. Making these omissions, the field is still extensive, for the co-operative form has been found to be extremely flexible and useful.

The functions to which the form has been applied, in the United States, are chiefly four:

1. By agricultural producers, for the processing or sale, or both, of their products.
2. By producers, for the purchase or manufacture of productive equipment and supplies.
3. By merchants, for the manufacture or purchase of their merchandise.
4. By consumers, for the manufacture or purchase and supply to them of all kinds of goods and services.

The first two functions are commonest in agriculture, and some of the associations that perform them are among the most successful existing merchants of agricultural products. Many of these same associations also produce or purchase for their members productive farm supplies, chiefly feed, seed and fertilizer. This part of their business is of long standing and well recognized. But in the last few years some of them have made a significant addition, the purchase for their members of general consumers' goods, and have thereby joined hands with the newer and smaller consumers' co-operatives in the cities, to the apparent benefit of both.

The reasoning is clear enough. We are members, let us say, of the Co-operative Creamery of Rolling Prairie, which has for years made good butter from our cream, and sold it to advantage. It has also purchased our requirements of feed and seed and fertilizer, and more

² The governing statutes are well collected in *WORKS PROGRESS ADMINISTRATION, ABSTRACTS OF THE LAWS PERTAINING TO COOPERATION* (1940).

recently of gasoline and oil, and we think it has saved us money, and given us good quality. But we must live as well as farm, and more than half of our expenditures for merchandise are for consumers' goods. Prices at the local store, we think, are high, and quality not always as expected. Why then should not our own association buy our household goods as well as farm supplies, on the same basis to which we are accustomed, and with like good results? And why not use the existing co-operative wholesale, which we and other creameries already own and use, for these new lines as well? And, since our costs per unit will decrease with volume, why not invite the local village people in? Why not indeed go further, and join hands with consumers in the cities, who are buying the same things through their own associations? Are we not all consumers? And, are not our interests, as consumers, all alike? We may dispute with people in the city about the price of butter, but on the price and quality of gasoline and clothing we are their friends and allies. Let us get together!

Thinking like this, and the resulting action, is increasing.³ Hard times enforce the argument, for slender incomes must be closely budgeted. And a war boom may not weaken it, for many incomes will not rise as fast as prices. Self-help and common action are both American traditions, and a workable idea that forwards both, on a wholly voluntary basis, without coercing anyone, has real elements of strength in a free country. We may properly expect the increase of the last few years both in membership and in variety of goods and services, to carry forward.

But the new goods and services bring unfamiliar legal problems, especially to the agricultural societies. Farmers for years have looked for higher prices for their products, and increasingly have sought and have received the aid of government. But so have other groups, both of producers and of merchants. Price-fixing laws for milk now find their parallel in the Bituminous Coal Act, and in fair trade acts fixing effective minima for many articles at retail. When a co-operative sells a price-fixed article, either on the farm or in the city, it meets price regulation at the other end. Must it adhere to the fixed price? And if it does, and makes a saving on its total operations, may it distribute that saving to its members on the basis of their patronage, or use it for

³ An estimate made by the Farm Credit Administration and reported by the Bureau of Labor Statistics, 52 MONTHLY LABOR REVIEW 1437 (1941), indicates that the purchasing business of farmers' co-operatives in the United States increased from \$5,000,000 in 1913 to \$358,000,000 in 1939-40. This includes only agricultural societies. The British experience is best reported in CARR-SAUNDERS, CONSUMERS' COOPERATION IN GREAT BRITAIN (1938).

their benefit in any other way? Or is a patronage dividend a rebate, and forbidden?

Selling at fixed prices is no hardship to a co-operative enterprise. Indeed to sell at market prices is a co-operative principle.⁴ No merchant knows his total costs on any item in advance, for part of cost is overhead, and overhead per unit depends on volume sold. Therefore, to try to sell at cost means bankruptcy. Co-operatives learned that lesson many years ago, and are content to make their prices at the market and divide the savings later if there are savings to divide. No co-operative therefore has protested very strongly against the decision in Wisconsin that special exemption from the prices set by manufacturers under the fair trade act is unconstitutional.⁵ But if that same act, or any of the other acts that sets a minimum on price, are held to forbid patronage refunds as well as price-concessions, the protest will be vehement.

And naturally so. For the co-operative is a self-help institution. Its members have joined it, to be sure, for a variety of motives. Some are religious people, and would like to practice on a week day the principles of brotherhood which they think about on Sunday. Some are humanist idealists and hope through co-operation to avoid exploiting others. Some dislike competition and are happier in a co-operative enterprise. Some look forward to the end of the capitalist order. But the motive that unites them all is that they are all consumers and hope as such by common action, without exploiting others, to improve their own position. For that purpose they have set up a business institution, financed it on a shoe string, done business according to the rules, endured the vicissitudes of business life, and finally have made a profit. If they were an ordinary corporation, they would invest part of that profit in their business, and distribute the balance among their stockholders, and no one would think for a moment of objecting. If one of those stockholders were also a customer of the business he would get his dividend just the same, whether or not the business dealt in price-fixed articles. The co-operative says: "We intend exactly the same thing, and you say we may not do it, solely because we have a different idea as to the basis of the distribution. Your reason is no reason. Our idea is as lawful and intelligent as yours; indeed we think it is more intelligent. We intend to distribute the profits of our business according to the law of our creation, and we claim the right to do so."

⁴ Warbasse, "Basic Principles of Cooperation," 191 ANNALS 7 at 9 (1937); UNITED STATES INQUIRY ON COOPERATIVE ENTERPRISE, REPORT OF THE INQUIRY ON COOPERATIVE ENTERPRISE IN EUROPE 21 (1937).

⁵ *Weco Products Co. v. Reed Drug Co.*, 225 Wis. 474, 274 N. W. 426 (1937).

What have the courts and Congress said about this proposition? Not very much as yet, but there are some analogies.

Congress first faced the question twenty years ago. The Packers and Stockyards Act, 1921,⁶ provides for public regulation of the charges of commission men on stockyards, and requires the lawful rates to be collected and retained. There were in existence at that time some co-operative associations selling livestock on commission. Section 306 (f) of the act⁷ provides that after rates have become effective

“ . . . no person shall . . . charge, demand, or collect a greater or less or different compensation for such services than the rates and charges specified in the schedules filed and in effect at the time; nor refund or remit in any manner any portion of the rates or charges so specified (but this shall not prohibit a cooperative association of producers from bona fide returning to its members, on a patronage basis, its excess earnings on their livestock, subject to such regulations as the Secretary may prescribe). . . .”

The same Congress, a year later, enacted the Grain Futures Act.⁸ The situation in grain was quite different. It was not proposed to regulate commissions upon grain exchanges, but to control speculation. To that end future trading was forbidden except on “contract markets,” and to become a contract market an exchange must do certain things. One of these related to co-operatives.

The situation was not hard to understand. Probably all commodities exchanges fixed commissions to be charged on brokered business, and forbade members to divide commissions with their customers. The latter rules were thought by some exchanges to exclude co-operatives from membership, because if they made any profits they would return part of them as patronage dividends. But Congress disagreed. By section 5 (2) of the act⁹ the Secretary of Agriculture was authorized to designate a board of trade as a contract market only:

“When the governing board thereof does not exclude from membership in and all privileges on such board of trade any duly

⁶ Act of Aug. 15, 1921, 42 Stat. L. 159 (1921), 7 U. S. C. (1934), § 181 et seq.

⁷ 42 Stat. L. 165, 7 U. S. C. (1934), § 207 (f).

⁸ Act of Sept. 21, 1922, 42 Stat. L. 998 (1922). The act was extensively amended in 1936 and now appears as the Commodity Exchange Act, 7 U. S. C. (Supp. 1939), § 1 et seq.

⁹ 42 Stat. L. 1000, 7 U. S. C. (1934), § 7 (e). Further provisions were added by the act of 1936, 49 Stat. L. 1499 (1936), 7 U. S. C. (Supp. 1939), § 10a. The original act was enforced against the Chicago Board of Trade in *Board of Trade v. Wallace*, (C. C. A. 7th, 1933) 67 F. (2d) 402, cert. den. *Wallace v. Board of Trade*, 291 U. S. 680, 54 S. Ct. 529 (1934).

authorized representative of any lawfully formed and conducted cooperative association of producers having adequate financial responsibility which is engaged in cash grain business, if such association has complied, and agrees to comply, with such terms and conditions as are or may be imposed lawfully on other members of such board: *Provided*, That no rule of a contract market shall forbid or be construed to forbid the return on a patronage basis by such cooperative association to its bona fide members of moneys collected in excess of the expense of conducting the business of said association.”

The Capper-Volstead Act of the same Congress¹⁰ authorized cooperative associations of agricultural producers, and defined them.

These three statutes, passed by a Republican Congress and signed by President Harding, seemed to establish the proposition that a cooperative association was a legitimate business agency, at least in agriculture, and that its most characteristic feature, the patronage dividend, was not to be destroyed by either public or private price-fixing. How has the principle fared in later legislation?

N. R. A. codes did not in all cases provide for fixing prices, but a good many of them did, and many forbade rebates and refunds. In only a few codes was there any special provision for the patronage refunds of co-operatives. The question therefore naturally arose whether they were forbidden. Reference to the President resulted in an executive order, October 23, 1933,¹¹ that

“ . . . no provision in any code of Fair Competition, agreement or license which has heretofore been or may hereafter be approved, prescribed or issued pursuant to Title I of the National Industrial Recovery Act shall be so construed or applied as to prohibit the payment of patronage dividends in accordance with law to any member by any bona fide and legitimate cooperative organization, including any farmers' cooperative, duly organized under the laws of any state, territory or the District of Columbia or of the United States, if such patronage dividends are paid out of actual earnings of such cooperative organization and are not paid at the time when such member makes a purchase from such cooperative organization.”

¹⁰ Act of Feb. 18, 1922, 42 Stat. L. 388 (1922), 7 U. S. C. (1934), §§ 291, 292.

¹¹ The date of course precedes the Federal Register and the order, like some more conspicuous orders of the same period, seems not to have been officially published. I derive the text from MAYERS, A HANDBOOK OF NRA, 2d ed., 310 (1934). “Bona fide and legitimate cooperative organizations” were further defined by an order of the Secretary of Agriculture, Dec. 31, 1934, text printed in UNIVERSITY OF WISCONSIN COLLEGE OF AGRICULTURE EXTENSION SERVICE, COOPERATION, PRINCIPLES AND PRACTICE 8 (1936).

The Robinson Patman Act¹² of course does not directly regulate prices, but forbids discrimination. It is hard to see how a legitimate patronage refund could be discriminatory, for all patrons, or at least all member-patrons, share in it pro rata. But Congress took no chances. Section 4¹³ provides that nothing in the act

“ . . . shall prevent a cooperative association from returning to its members, producers, or consumers the whole, or any part of, the net earnings or surplus resulting from its trading operations, in proportion to their purchases or sales from, to, or through the association.”

It will be noticed that this, like the President's order under the N. R. A., is no longer limited to agricultural co-operatives, but clearly includes organizations of consumers also.

The story now passes to the states. Beginning with a California act in 1931,¹⁴ prodded by a strong retail druggists' lobby, and aided by a decision of the Supreme Court in 1936¹⁵ and by the Miller-Tydings Amendment to the Sherman Act in 1937¹⁶ forty-four states had enacted "Fair Trade Acts" by the end of 1939.¹⁷ These acts make it lawful for a distributor of trade-marked articles to fix by contract the price at which his goods are to be resold at retail by his customers, and forbid concessions from the fixed price by any merchant who acquires the goods with notice, whether or not he is a party to the contract. Do these laws forbid patronage refunds by co-operatives?

Most of them say nothing on the subject. The Wisconsin act undertook to exempt co-operative associations entirely,¹⁸ but as we have seen that section was held invalid by the Supreme Court of Wisconsin.¹⁹ Only the Michigan act contains a clear provision for the patronage refunds of co-operatives, and it is limited to farm organizations.²⁰ This

¹² Act of June 19, 1936, 49 Stat. L. 1526 (1936), 15 U. S. C. (Supp. 1939), § 13 et seq.

¹³ 49 Stat. L. 1528 (1936), 15 U. S. C. (Supp. 1939), § 13b.

¹⁴ Cal. Laws (1931), p. 583, now Cal. Gen. Laws (Deering, 1937), act 8782.

¹⁵ *Old Dearborn Distributing Co. v. Seagram Distillers' Corp.*, 299 U. S. 183, 57 S. Ct. 131 (1936).

¹⁶ Act of Aug. 17, 1937, 50 Stat. L. 693 (1937), 15 U. S. C. (Supp. 1939), § 1.

¹⁷ The texts of these acts as of 1940 are collected in *WORKS PROGRESS ADMINISTRATION, STATE PRICE CONTROL LEGISLATION (1940)* (Marketing Laws Survey series, vol. 2).

¹⁸ Wis. Stat. (1937), § 133.25 (8), enacted in 1935.

¹⁹ *Weco Products Co. v. Reed Drug Co.*, 225 Wis. 474, 274 N. W. 426 (1937).

²⁰ Mich. Pub. Acts (1937), No. 50, § 3, Stat. Ann. (Supp. 1941), § 19.323: "The payment of patronage dividends by farmers' cooperative associations or companies on the basis of sales of commodities sold under the provisions of this act shall not be construed as a violation of the provisions of this act."

silence is extraordinary, for substantially all these states had laws on the books authorizing co-operatives, and providing for patronage refunds.²¹ I will try later to assess the meaning of it.

The statutory story is concluded with the Bituminous Coal Act of 1937.²² That act authorizes the fixing of minimum prices and contains elaborate provisions against rebates and discounts.²³ But members of the code may sell "to or through any bona-fide and legitimate farmers' cooperative organization . . . whether or not such organization grants rebates, discounts, patronage dividends, or other similar benefits to its members."²⁴ Again the reference is to *farmers'* organizations only. But whereas in the legislation of 1921 and 1922 the important thing was selling, and the exemption interested farmers only, this law deals with buying, and there the farmer is no different from his brother in the city. If any exemption is proper, or is needed, it should apply to both.

The question then recurs: What is the position of a consumers' co-operative under this legislation, or of any co-operative under the state fair trade acts outside Michigan? That will depend on what a patronage dividend is. If it is a price-reduction (whether called rebate, refund, or by whatever name) it seems to be forbidden, for minimum prices are the chief objective of these laws. But perhaps it is something quite different, namely a distribution of the earnings of a business among the persons entitled to receive them. That makes a different story.

Sometimes an analogy is useful. Industrial companies may lawfully invest in railroad stocks.²⁵ Let us say the *X* Steel Company owns stock of the *Y* railroad, on which it is a shipper. Of course it pays the tariff rates, like everybody else. But the railroad makes a profit, and declares a dividend. The policy and law forbidding railroad rebates is at least as stringent as that against reduction in the quoted price of coal or aspirin or whiskey. But does anybody doubt that the steel company may participate in the railroad's dividend, although it is a shipper? And would it make any difference if all the railroad's stockholders were

²¹ The acts are collected in WORKS PROGRESS ADMINISTRATION, ABSTRACTS OF THE LAWS PERTAINING TO COOPERATION (1940).

²² Act of April 26, 1937, 50 Stat. L. 72 (1937), 15 U. S. C. (Supp. 1939), § 828 et seq., extended by Act of April 11, 1941, c. 64, Pub. L. 34.

²³ 50 Stat. L. 77, Part II, § 4 (1937); 15 U. S. C. (Supp. 1939), § 833.

²⁴ 50 Stat. L. 77, Part II, § 4 (i) (13) (1937); 15 U. S. C. (Supp. 1939), § 833 (i) (13).

²⁵ *United States v. Elgin, Joliet & Eastern Ry.*, 298 U. S. 492, 56 S. Ct. 841 (1936).

shippers? Or if all shippers who desired to join in ownership might do so? Or if the distribution were in proportion to their shipments?

The truth is that a patronage dividend is not a price reduction on any given sale. It cannot be allowed or promised when a sale is made, for it is made from earnings only, and no one can be sure there will be any earnings. Our business may sell at an eighty per cent mark-up and still go broke if overhead exceeds that spread. And we will not know our overhead per unit until we know our total volume. Neither will we know our bad debts, or other losses. We may make shrewd guesses, and quite close estimates of earnings if we know our business well, but we cannot be sure, and therefore we can never promise. The Secretary of Agriculture put his finger on the heart of this matter in his definition of "bona fide and legitimate co-operative organizations" for purposes of N. R. A.²⁶ A co-operative is bona fide, said the Secretary only if it

" . . . does not distribute such [patronage] dividend in the form of a refund at the time of purchase; and does not evidence any such dividend by any agreement or representation to distribute any definite or specified dividend."

If any business violated this, anyone would rule that it was selling at a discount. Such discounts come before net earnings, not thereafter. Whether evidenced by trading stamps or otherwise, they are subtractions from gross income, not divisions of net profit.

True patronage dividends are divisions of net earnings.²⁷ Net earnings are not made on any single sale. They result from the total operations of some accounting period, and become known only after all the results for that period are in. A distribution of them, on whatever basis, is not a price reduction nor a rebate, and is not made unlawful by price-fixing legislation. Co-operatives, like other business units, have a right to distribute their net earnings in accordance with the law of their creation. Until some statute forbids that, bona fide patronage dividends are entirely lawful.

²⁶ Order of Secretary of Agriculture of Dec. 31, 1934, text printed in UNIVERSITY OF WISCONSIN COLLEGE OF AGRICULTURE EXTENSION SERVICE, COOPERATION, PRINCIPLES AND PRACTICE 8 (1936). The President's order is equally explicit. Executive Order of October 23, 1933, quoted in MAYERS, A HANDBOOK OF NRA, 2d ed., 310 (1934).

²⁷ And it does not matter whether the particular association prefers to call them "profits," "proceeds," "earnings," "savings," or whatever. For some purposes these distinctions make a difference. See, e.g., O'Meara, "The Federal Income Tax in Relation to Consumer Cooperatives," 36 ILL. L. REV. 60 (1941). But for this purpose the important point is that they are *net*.