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CALIFORNIA FAIR TRADE ACT.*

BY IRA J. DARLING, M.A., LL.B.[1,2]

The anti-trust law of California, passed in 1907, is popularly known as the Cartwright Act. In the act a trust is defined to include a combination to increase the price or prevent competition in the sale of merchandise or to fix any standard or figure, whereby its price to the public or consumer shall be controlled. (Stats. 1907, page 984, ch. 530.) Such a trust is forbidden and very severe penalties are prescribed.

Statistics are not readily available to show what attempts were made to enforce the California anti-trust law in the two years following its enactment, but it is doubtful whether it was ever sternly enforced in all its rigor.

In its original form the California anti-trust law absolutely forbade any kind of a price setting agreement. It was clearly based upon the economic theory that the general welfare would be promoted by free and unlimited competition. It was enacted at a time when it was believed that an industrial system saturated with competition would automatically result in well-equipped factories, an efficient system of distributing the manufactured products and room for an unlimited number of small retail outlets with an ever-increasing rate of turnover. The law of supply and demand was considered adequate to adjust prices. *Laissez-faire* was the slogan.

In some magical way the energetic California competition was to make it possible for all the retail outlets, the numerous small drug stores as well as the large ones, to have customers who had the purchasing power to maintain indefinitely a high rate of turnover with a healthy mark-up. Now these California customers were mainly people with pay envelopes, salary checks or those receiving incomes

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from rents or interest. The amount received by customers in wages, salaries, rent and interest was not equal in amount to the selling price of the articles offered for sale. It was not equal to the selling price, never has been, and the California Legislature, by the enactment of an anti-trust law could not make it equal. The amount received in wages, salaries, rent and interest not being equal to the total selling price of the products offered for sale, some of them, obviously, had to remain unsold, and there was "overproduction," or, to state it more accurately, there remained the lack of purchasing power.

Furthermore, the larger concerns who had reserves of capital and had access to favorable markets began cutting prices in order to get rid of their stock. The small stores, of course, had to cut prices likewise to meet the competition, but many stores, especially the small ones, could not afford to take the loss and failed.

When the California Legislature met in 1909 it was faced by the ever present and sorrowful fact that purchasing power did not equal selling price, and that good management and lusty competition had not succeeded in making it equal. At that session the Legislature decided to reverse some of its economic theories in order to try to solve the chronic problem that has driven sales managers to early graves while production managers have been able to take merited vacations. So, in 1909, there was adopted a sweeping amendment to the Cartwright act of doubtful constitutionality. In part the amendment provided ". . . No agreement, combination or association shall be deemed to be unlawful . . . the object and business of which are to conduct its operations at a *reasonable profit* or to market at a reasonable profit those products which cannot otherwise be so marketed. . ." (Stats. 1909, page 593, ch. 362.) In other words, if a contract sets a minimum resale price, and it merely assures a reasonable profit, and if there is no other way of selling the product at a reasonable profit, then the contract is lawful. But what did the Legislature mean by a "reasonable profit?" Similar words in a Colorado statute were held to be so vague as to be unconstitutional, in the opinion of the United States Supreme Court in 1927. (Cline *vs.* Frink Dairy Co., 274 U. S. 445, 47 Sup. Ct. Rep. 681.) However, in the eighteen years intervening, the constitutionality of the 1909 amendment was not questioned by the California courts.

If the "reasonable profit" amendment of 1909 was unconstitutional, then it is probable that the original anti-trust law remained in effect. However, the California courts construed the anti-trust law as though the amendment were valid so as to permit contracts for what was claimed to be a reasonable profit.

The anti-trust law of 1907, the "reasonable profit" amendment of 1909 and the several bulky volumes of fine-printed statutes since then had all failed to usher the hard working retail druggist of California into the golden land of eternal prosperity where red ink is unknown. In 1931 the rate of turnover was not what it should be; it was hard to maintain a respectable mark-up. Customers just didn't seem to buy enough goods at the proper prices. Sometimes it was hard to pay the rent. Many small stores resorted to bankruptcy and the bankrupt stock was bought up and sold by some of the inconsiderate chain stores at cut-throat prices, even below the wholesale price.

The Legislature sought to remedy this situation in 1931 by the passage of the Fair Trade Act (Stats. 1931, page 583, ch. 278), which definitely abandons the "reasonable profit" test, and makes resale contracts legal regardless of whether or

not the price named is one that will render the buyer or seller a reasonable profit, or more or less than a reasonable profit, or none at all. Such contracts need not be limited to forms of business that cannot otherwise be conducted at a profit. The California Fair Trade Act provides in part:

"No contract relating to the sale or resale of a commodity which bears, or the label or content of which bears, the trade-mark, brand, or name of the producer or owner of such commodity and which is in fair and open competition with commodities of the same general class produced by others shall be deemed in violation of any law of the State of California by reason of any of the following provisions which may be contained in such contract:

"1. That the buyer will not resell such commodity except at the price stipulated by the vendor.

"2. That the vendee or producer require in delivery to whom he may resell such commodity to agree that he will not, in turn, resell except at the price stipulated by such vendor or by such vendee.."

Perhaps the troubles of the retail merchant were over. Perhaps!

In spite of the Fair Trade Act of 1931, sad but stern history tells us that prosperity did not come to California in the two years following 1931. By the time the Legislature of 1933 met it was painfully evident that the Fair Trade Act had not ushered in an era of abundance. As far as the retailer was concerned prosperity was still "around the corner," and he had decided that the world was at least an octagon.

One trouble seemed to be that the contract signed by the manufacturer and retailer was binding on no one except the parties who signed it. There were many ways of evading the purpose of the Act.

A competitor of the person violating the contract could not take any action to enforce it. The contract could not be enforced by some one who had not signed it, unless it stated that it was made for the benefit of that person, and it could not be enforced *against* some one who had not signed it. It was simply a private arrangement between the contracting parties.

The California Legislature is very obliging. It never hesitates to correct the mistakes of earlier legislatures or to change its economic theories when necessity seems to demand it, provided, of course, that there is no powerful pressure-group with a well-organized lobby opposing the change.

The theory was advanced by the retail druggists' lobby and others that the Fair Trade Act needed some "teeth," that it should be made easier to wreak legal vengeance upon some one when a duly signed Fair Trade contract failed to get the desired results, that possibly the highway to retail prosperity could be made smooth by paving it with lawsuits!

In 1933 the Legislature amended the California Fair Trade Act by adding the following section:

"Section 1½. Wilfully and knowingly advertising, offering for sale or selling any commodity at less than the price stipulated in any contract entered into pursuant to the provision of section 1 of this act, whether the person so advertising, offering for sale or selling *is or is not a party to such contract*, is unfair competition and is actionable at the suit of *any person damaged thereby*." (Stats. 1933, page 793, ch. 260.)

Thus it is seen that the 1933 amendment to the Fair Trade Act authorizes an action to enforce a contract between a manufacturer or a wholesaler and the

retailer against anyone who "wilfully and knowingly" violates it, even though the party had not signed the contract. The person bringing the action need not be a person who has signed the contract, but may be any person damaged by the breach thereof. The amendment appears to declare that a private price fixing contract entered into between a manufacturer or wholesaler and a retailer may take on a status approaching that of a law binding upon every one else who knows about it.

The constitutionality of the 1933 amendment has not been definitely decided. There is no Federal decision or other state Supreme Court decision in point because there is no other statute similar to the California statute to be construed. The cases that have arisen in this state under the Act have not yet been decided by the California Supreme Court. One of these cases is now before the Court but no decision has been rendered. There have been trial court decisions upholding the amendment and decisions declaring it unconstitutional. Notice will be taken of three decisions in the trial courts.

Since there is no direct precedent for the 1933 amendment the courts are not in a position to follow an established precedent; moreover, it is impossible for the attorneys before a court to prove positively what the effect of the amendment would be, for the simple reason that the fact does not yet exist. If the court can decide the case on neither proof nor precedent, then it must theorize. If so, the decision will depend upon the economic theories of the particular judge or judges who hear the case.

In each of the California cases the plaintiff was a manufacturer or distributor who had signed a Fair Trade contract with various retailers. However, in each case the defendant was a retailer who had refused to sign one of plaintiff's contracts and was selling at a price lower than that named in plaintiff's contracts.

In the case of *Max Factor & Co. vs. Clarence G. Kunsman,*[1] decided in October 1933, by Judge Emmet H. Wilson of Los Angeles, it was held that the 1933 amendment violated both the California and the United States constitutions. The court considered the amendment an attempt to legislate under the police power, but held that the amendment had no reasonable and necessary connection with the public welfare. The court says,

"The right of the owner to sell his property at a price satisfactory to himself 'is an inherent attribute of the property itself,' and is within the due process clause of the Fifth and Fourteenth amendments to the Constitution of the United States."

The court further states:

"A legislative enactment undertaking to regulate useful business enterprises is subject to review by the courts with a view of determining whether it is a lawful exercise of the police power, or whether under the guise of police regulations there has been an unwarranted interference with the constitutional right to carry on a lawful business, to make contracts, or to use and enjoy property."

In summing up the case against the 1933 amendment the court says:

"It necessarily follows that section $1\frac{1}{2}$ of the Fair Trade Act is in violation of the Fifth and Fourteenth amendments to the Constitution of the United States, and in violation of the Constitution of California, in that it deprives persons of their property without due process of law and without compensation, it abridges the privileges and immunities of citizens, it deprives them of the full and free use of their property, it imposes an unlawful, unnecessary and unreasonable restraint

[1] See text of opinion, *The Los Angeles News,* October 21, 1933.

upon the alienation of property and upon contracts, and it is an unlawful interference with private business. It is not a valid exercise of the police power and it is not for the protection of the peace, health, safety, morals, or *welfare of the public.*" (*Italics mine.*)

This decision is a good expression of the older economic theories relating to property and contract rights. The court takes the view that the public welfare demands hands off from private property and non-interference with business competition, at least so far as the retailing of cosmetics is concerned.

In *Weco Products Company of California vs. Sunset Cut Rate Drug Co.*,[1] decided in January 1934, by another Judge of the Superior (trial) Court, the amendment was held constitutional. The court did not devote very much space in its opinion to the knotty problem of "public welfare," not approaching that indefinite theory nearer than to say, ". . . the legislative body is presumed to be guided by proper considerations of public policy. . . ." Most of the opinion is devoted to the argument that the amendment is valid on the theory that it was passed to protect the manufacturer or distributor, that is, to protect his system of contracts, good will, trademarks, etc. The defendants by their conduct were inducing other people who had signed contracts to break them.

Parties to a contract traditionally have been given some protection against third persons coming in and inducing the other person to break the contract. But never before has it been held that mere price cutting by the third party was the kind of conduct which would make him liable. However, in no other case decided on the theory of protecting contracts against the actions of third parties has there been a statute declaring price cutting unlawful. In this state under the Fair Trade Act if the defendant's actions are unlawful, they are unlawful because of the statute and not because the contracts are injured. Therefore it would seem that the court's reliance upon the legal theory that the plaintiff has a right of action because of an unlawful invasion of his contract is not sound. It cannot be logically advanced that the breaking of the contract because of fear of competition is an unlawful invasion of contract right on the part of the third party competitor, unless it can be held to be constitutional for the Legislature to give private contracts the status of law which cannot be broken.

In the Weco case the court in its opinion barely referred to the "public welfare," and made no reference to the welfare of the retailers.

This case would not be precedent for the constitutionality of that part of the Act which states that "anyone injured thereby" can sue.

If the Supreme Court should decide that the manufacturer has property rights remaining to him in trade-marked articles which he can protect against any price cutting then he, but not the retailers, would have a legal remedy.

The last decision to be particularly noticed in this paper is the case of *General Cigar Co. vs. The Drug Market*,[2] decided in the Superior Court, in September 1934. In holding the amendment constitutional the court said, "It is in evidence before me . . . that the underselling of branded and trade-marked articles has resulted in the bankruptcy of hundreds of small independent dealers, leaving in its wake unemployment and economic distress," and it "is a fair exercise of the police power

[1] See text of opinion, *West Coast Druggist*, February 1934, page 8.

[2] See text of opinion, *The Los Angeles Daily Journal*, September 28, 1934.

. . ." The court took the view that the amendment was enacted to aid the retailer directly, and indirectly to promote the public welfare.

The older view of police power was that it extended only to public *health, safety* and *morals*. The court in the General Cigar case takes the newer view that the police power extends also to some field, as yet poorly defined, that is sometimes termed "public welfare," and sometimes called "economic welfare, public convenience and general prosperity of the community." In support of the view that the police power extends to the economic sphere the court quotes at length from the case of *Nebbia vs. New York* (March 1934), 291 U. S. 502, 54 Sup. Ct. Rep. 505:

> "If the law-making body within its sphere of government concludes that conditions or practices in an industry make unrestricted competition an inadequate safeguard of the consumer's interests, produce waste harmful to the public, threaten ultimately to cut off the supply of a commodity needed by the public, or portend the destruction of the industry itself, appropriate statutes passed in an honest effort to correct the threatened consequences may not be set aside because the regulation adopted fixes prices reasonably deemed by the legislature to be fair to those engaged in the industry and to the consuming public."

The *Nebbia* case clearly shows that the police power now extends to economic affairs, but it must be noted that the prices in the *Nebbia* case were fixed by the government itself.

As an additional ground for upholding the 1933 amendment the court in the *General Cigar* case advances the following theory ". . . where the goods are well advertised and branded, a manufacturer has an interest, or concern, if you like, in those goods which are identified by his marks and advertisements." The court places great weight on the New Jersey case of *Robert H. Ingersoll & Bro. vs. Hahne & Co.*, 89 N. J. Eq. 332, 108 Atl. 128. New Jersey passed a statute making it unlawful to "discriminate against (a trade-mark) by depreciating its value," etc., except where the goods did not carry a notice forbidding such practice. The plaintiff marketed a popular brand of watch bearing a notice and trade-mark, the notice being construed by the court as a contract. The notice or contract provided that the retailer was licensed to use the *trade-mark*, etc., provided the watch were not sold for a price other than $1.35. The retailer could remove the notice and *trade-mark* and sell the watch at any price that he chose; but without removing the trade-mark and notice this particular defendant offered the watches for $1.00. The court held it unlawful for the defendant to do so, and held the New Jersey statute constitutional. But it is to be noted that the New Jersey contract did not set a price on the *article itself* as do the contracts authorized by the California statute. Possibly some courts would be inclined to distinguish between the two statutes.

It will be very interesting to read the opinion of the California Supreme Court, and ultimately an opinion from the United States Supreme Court.

The court says, in the *General Cigar* case, "It is a matter upon which only the opinions of the highest court in the state and nation can be of practical interest to the litigants, their counsel and the commercial world in general." In the meantime, we must be guided—and confused—by the decisions of the trial courts, and since these decisions are in direct conflict one with another, we can only guess what the law will ultimately prove to be.

Will a judicial opinion upholding the validity of the 1933 amendment to the Fair Trade Act solve the problem? At their best such contracts are very difficult

and expensive to enforce.[1] One user of Fair Trade contracts plaintively writes "... We cannot sue 200 or 300 retailers. Frankly, the legal expense is beyond our means..."[2]

Possibly, after all this legal travail, many retailers will place slight reliance on Fair Trade Acts, amendments, injunctions, voluminous briefs and learned but conflicting judicial decisions. We find editorial reference to the " . . universal complaint of Fair Trade manufacturers that retailers are not showing enough interest in the Act to return contracts, and the lack of support of Fair Trade items by retailers; the apparent divided opinion on the part of manufacturers regarding the advisability of refusing to sell retailers who do not sign Fair Trade contracts."[3]

There is no provision in the Fair Trade Act that the minimum retail price named in the contract shall be high enough to insure a profit to the retailer.

There is no requirement that products be sold to all retailers at the same price.

There are many types of disastrous competition that cannot be reached by Fair Trade legislation. It does not limit the *producing* units—factories, laboratories, etc., with duplicating machinery. It does not limit the number of *distributing* units with their duplication of facilities. Nor does it limit competition between substantially the same product under an unlimited number of trade names. It does not limit the number of competing retail stores, as new stores are permitted to open at any time regardless of the public need for such stores.

More sweeping legislation is needed to correct the difficulties confronting the retail druggist.

THE PLACE OF COMMERCIAL SUBJECTS IN THE PHARMACY CURRICULUM.*

BY NEAL B. BOWMAN.[1]

No one will deny the fact that there is an ever-increasing trend toward specialization in almost every field of endeavor. Therefore, it is not surprising to find that the drug business is concerned with various proposals concerning its possible reconstruction. This reconstruction was given impetus by the increase in course requirements and the demands brought about by changes in the business relations of the pharmacist, and the question suggests itself, "What is the place of commercial subjects in the pharmacy curriculum?"

Each teacher of commercial subjects, quite naturally with intellectual honesty, will champion his own subjects, feeling justified in so doing by virtue of the fact that he is the one charged with the responsibility of teaching those subjects.

Society is so constituted that every member of it, after he has passed his

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[1] Blumenfeld, Juliet, *Retail Trade Regulations and Their Constitutionality*, 22 California Law Review, page 86.

[2] L. B. Laboratories, Inc., "An Open Letter to the Druggists of California," *West Coast Druggist*, April 1935, page 17.

[3] *West Coast Druggist*, July 1934, page 12.

* Section on Commercial Interests, A. PH. A., Portland meeting, 1935.

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