CHAPTER 10

RESTRICTIVE BUSINESS PRACTICES

BEFORE the war there were few industrialized countries, outside of the United States, in which the production and sale of manufactured goods were effectively competitive. In Japan, where industrialism had been imposed upon a feudal society, the control of industry was in the hands of a few great families. In Germany, France, Italy, and elsewhere on the continent of Europe, the control of major industries was concentrated in giant combines and the production and distribution of manufactured goods were regimented by powerful cartels. Through these agencies European business fixed prices and terms of sale, divided productive activities, markets, and customers, limited production, assigned quotas in output and sales, and enforced its regulations by the imposition of penalties. In Great Britain, where the policy of freedom of trade had long impeded the progress of cartelization by compelling British businessmen to meet the competition of foreigners, the abandonment of that policy, following the First World War, provoked a rapid transition to a predominantly cartelized economy. British trade associations, on the eve of the Second World War, were busily engaged in fixing prices, buying up and retiring productive capacity, limiting output, assigning quotas, pooling earnings, and using these pools to reward those who restricted output and to penalize those who increased it.

The consequences of such cartelization are clear. By establishing prices at levels that are calculated to cover the costs of their least efficient members, cartels remove the incentive to introduce improvements and eliminate wastes. By assigning quotas on the basis

of present capacity or past output, they freeze production to existing locations and obstruct adjustments that might cut costs. In both of these ways they operate to maintain capacity in idleness, to curtail production, and to prevent consumption from reaching levels which it might otherwise attain. Instead of facilitating economic progress, they make for stagnation and decay.

These restraints within domestic markets have their counterparts in the restrictions that producers have imposed on international trade. In fact, the two are intimately related. For, unless high tariffs and shipping costs prevent it, monopolistic arrangements in domestic markets may be destroyed by competition from abroad. And, unless domestic markets are effectively controlled, international monopoly may be destroyed by competition at home.

The tightest form of control over world markets is that accomplished through the international combine. In this case, the holding company device is commonly employed to bring under common ownership and management a number of enterprises that have been incorporated to operate in different countries. A looser form of organization than the combine, the international cartel may be equally effective in eliminating competition in world trade. Price-fixing cartels have controlled the rates charged for international services and pegged the prices of goods sold in world markets. Territorial cartels have distributed exclusive sales areas among their participants. Quota cartels have curtailed production and exports and allocated output and export shares. Selling syndicates have handled foreign orders, fixed prices, and apportioned sales. Patent cartels have operated international patent pools, including in their licenses provisions which have enforced a parcellation of the markets of the world.

Like the domestic cartel, the international cartel operates to bar new enterprise, to obstruct technological improvement, to impair productive efficiency, to check consumption, and thus to hold down planes of living. Like the tariff, it operates to restrict trade. But, unlike the tariff, it is set up by businessmen, without public representation or responsibility, for private ends. It thus usurps the authority of governments and delivers the determination of foreign economic policy into private hands.

The effort to expand trade by reducing tariffs and eliminating quotas might well be defeated if no action were taken to prevent the erection of private tariff and quota systems by international cartels. The necessary action might either be taken through international agreement or left to the initiative of individual states. But unilateral action, even when taken by a government as powerful as that of the United States, has its limitations. It cannot protect domestic consumers against the consequences of cartel agreements in which domestic producers do not participate. It cannot obtain evidence concerning agreements made and administered abroad, even where domestic producers do participate. And if it does succeed in breaking up a cartel that is sponsored or supported by other governments, it may induce those governments, in one way or another, to retaliate. If action against restrictive business practices in international trade is to be effective, it must be taken by many states in accordance with a common understanding as to policy. If the tariff and quota provisions of the *Charter* were not to be evaded, it was therefore important that such an understanding be obtained.

APPROACHES TOWARD CARTEL POLICY

In its domestic market, the United States has adopted two contrasting policies in dealing with the problems of monopoly. In the case of industries "affected with a public interest," such as transportation and public utilities, it has permitted monopolies and set up administrative agencies to regulate their practices. In the case of other industries, it has sought to preserve competition by forbidding the establishment of monopolies and by breaking them up where they exist; it has maintained machinery for the enforcement of these measures and sought to induce compliance by providing for the imposition of penalties. Where action in international markets must be taken by an intergovernmental agency, it is impossible, under present conditions of political organization, to follow either of these policies.

The method of administrative regulation, even when applied to a single enterprise operating in a local market, is always difficult and often ineffective. Applied to many enterprises operating in world markets, it would encounter problems of baffling complexity. To be

effective, it would require powers that no nation is now prepared to surrender to an intergovernmental agency. Such regulation, therefore, is not feasible either economically or politically.

The method of anti-trust is also unavailable. Even in the United States, the meaning of "restraint of trade" has never been precise. In international negotiations, agreement upon definitions of practices that would be held illegal by all countries under all circumstances is not to be obtained. Nations differ in economic development and organization, in constitutional requirements, legal systems, and administrative procedures, and in their traditional attitudes toward competition and monopoly. Few of them have ever embraced the American philosophy of anti-trust. None of them is prepared to confer upon an intergovernmental agency the powers required to break up existing cartels or to prevent new cartels from being formed. Action to preserve competition in international trade must be taken by individual governments. And it must rest upon the voluntary cooperation of national states.

If world trade is not to be restricted by private agreements, a workable method of intergovernmental action must be found. Such a method was suggested in the American *Proposals* and elaborated in the draft of the *Charter* first prepared by the United States. Under this plan, governments would agree to take action, individually and collectively, to curb restrictive business practices in international trade. They would also agree to the enumeration of certain practices which might be held to be restrictive in their effects. These practices would be judged, not by their form, but by their influence on the volume of trade and industrial activity. Any member might complain that the practices followed, under a particular agreement, did, in fact, operate to restrict trade. The ITO would then investigate the charge and, if it were substantiated, would recommend remedial action to the governments concerned. A common policy was thus established; an instrument was provided to aid in its effectuation; enforcement was left to member states.

ISSUES IN THE CARTEL NEGOTIATIONS

There was no opposition at London, Geneva, or Havana to including in the *Charter* a chapter on restrictive business practices.

There was acceptance, in general, of the American approach. But there were sharp differences of opinion as to many of its details. On individual issues, Canada frequently sought tighter provisions than those proposed by the United States; the United Kingdom, Belgium, and the Netherlands usually sought looser ones. The undeveloped countries, as consumers of cartelized goods and services, generally gave their support to Canada and the United States. In some respects the resulting chapter is weaker, in others stronger than that contained in the original American draft.

One American proposal would have established a presumption as to the restrictive effects of certain practices and imposed the burden of proof on those accused of using them. It was argued, in opposition to this proposal, that it would be both unfair and incompatible with recognized principles of civil law to incorporate an *a priori* condemnation of such practices and it was insisted that reliance should be placed on the development over time of a body of standards growing out of specific findings of the ITO. This view prevailed and the proposal was dropped.

The American text would have required members to "take action" to carry out the recommendations made, in particular cases, by the ITO. It was objected that this requirement would impose unequal obligations on different governments. In the United States, for instance, the government might "take action" by submitting evidence to a grand jury or by seeking an injunction from a court. Neither the grand jury nor the court, however, could be required to accept the findings of the ITO. In certain other countries, on the contrary, business is not protected by "due process of law"; governments have power to intervene directly in industry; a commitment to "take action" would require them to carry out any recommendation that the ITO might make. It was agreed, accordingly, that each member should take full account of the Organization's specific recommendations in determining what it should do to carry out its general obligation in a particular case.

Under the American draft, private citizens or business entities could have carried complaints directly to the ITO. In criticism of this provision, it was said that governments cannot be asked to answer to complaints made, not by other governments, but by their

nationals. In the present text it is therefore provided that governments must take responsibility for the filing of complaints.

In other respects, however, the American proposals were improved upon. The *Suggested Charter* would have applied the procedure of complaint, investigation, and recommendation only to practices that might be proven to be restrictive by their past effects. It was pointed out that the procedure, if thus limited, might operate to cure past abuses but could not be used to prevent future ones. The text was therefore amended to permit the application of the procedure not only to practices that have had restrictive effects, but also to practices that are about to have such effects. Under the present wording, a complaint may be lodged against a cartel agreement as soon as it is made.

One of the points most vigorously disputed during the negotiations was the application of the provisions of the chapter to state-trading enterprises. Under the text adopted at London, a complaint regarding restrictive practices involving several concerns could be brought against both public and private commercial enterprises, but complaints regarding the restrictive practices of a single concern could be brought against private enterprises alone. At Geneva, public enterprises were brought within the scope of the latter category of complaints. At Havana, determined efforts were made by Mexico and Argentina to exempt state enterprises from some or all of the provisions of the chapter. These efforts, however, were unsuccessful; the coverage established at Geneva was retained.

Another controversy followed a proposal to extend the chapter's procedures to international transportation, communications, insurance, and commercial-banking services. This move was supported by many of the undeveloped countries and opposed by the principal maritime powers. The opposing views of these two groups were finally compromised by excluding from the chapter services that fall within the jurisdiction of other intergovernmental organizations and applying a simpler procedure in the case of any that may remain.

A final issue was raised by a British contention that, in any case involving restrictive business practices, a member should be required to exhaust the procedures of the chapter relating to such practices

before it could ask the ITO to release it from obligations toward another member on the ground that benefits promised it by that member under the *Charter* had been nullified or impaired. Since the nullification and impairment procedure is the means of applying the only sanction provided for the enforcement of the *Charter,* this contention threatened to weaken the whole structure by delaying its use. Fortunately, it was rejected; if commitments are violated, the procedure set up for the investigation of restrictive business practices cannot be interposed.

CARTELS IN THE CHARTER

Each member of the ITO will agree to "take appropriate measures . . . to prevent . . . business practices affecting international trade which restrain competition, limit access to markets, or foster monopolistic control, whenever such practices have harmful effects on the expansion of production or trade and interfere with the achievement of any of the other objectives" of the *Charter.* This commitment covers practices, within the member's jurisdiction, engaged in by one or more private or public commercial enterprises whenever such enterprises, individually or collectively, "possess effective control of trade among a number of countries in one or more products." It does not apply to practices outside the member's jurisdiction or to those confined to local markets; it does not apply to the practices of competitive enterprise; it is concerned with the problem of monopoly in international trade (46–1, 2).

To make this policy effective, two procedures are provided. Members affected by restrictive business practices carried on by enterprises located in other countries may ask the ITO to arrange for consultation with such countries in order that the situation may be remedied (47). Alternatively, or as a further resort, a member may submit a written complaint directly to the ITO. If a preliminary screening indicates that the complaint may have substance, the Organization will investigate. In such an investigation, it will collect further information from member governments and may hold hearings at which representatives of governments, business entities, and private citizens will be given an opportunity to appear. The Organization will then make a finding as to whether the practices

in question have had, or are about to have, harmful effects. If such effects are found, the ITO will notify all member governments, call upon them to take appropriate measures to prevent the continuance or recurrence of the practices, and, at its discretion, may recommend specific remedies. The Organization will publish the record of the case and, from time to time, report upon the action taken by member states. Where the practices of a single public enterprise are questioned, an attempt must be made to correct the situation through consultation before a complaint is formally submitted to the ITO (48).

The *Charter* enumerates the specific practices that will be subject to complaint. These include such practices as fixing prices or terms of purchase or sale; discriminating against particular enterprises or excluding them from markets; allocating markets, production, customers, sales, or purchases; curtailing output or fixing production quotas; agreeing to prevent the development or application of technology; and extending the use of rights acquired under patents, trade marks, and copyrights to products or activities which are not within the scope of such grants. This list is comprehensive; it cannot be extended without a two-thirds vote of the Organization's membership (46–3).

Two of the items in the list require further comment. Alleged suppression of technology is not to be investigated unless a conspiracy among potential competitors is involved. The practice is so described as to exclude deferment of application by a single enterprise. The ITO, moreover, is given no authority to pass upon the legal scope of patents, trade-marks, or copyrights. This determination, under the present wording, must be made under the laws of the countries that have made the grants. Both of these provisions were clarified at Geneva in response to suggestions made in hearings before the United States Senate Committee on Finance.

Each member of the ITO will be required to "take all possible measures, by legislation or otherwise," to carry out its general obligation to suppress restrictive business practices. It need not accept specific recommendations made in particular cases by the ITO. But it must take such recommendations into full account in determining, "in accordance with its constitution or system of law and economic

organization," what action it will take. If a member does not take the recommended action in a particular case, it must explain its inaction to the ITO and discuss the matter further if the Organization so requests (50).

This, in its major outline, is the method proposed to curb restrictive business practices. The *Charter* also provides that its procedures shall not be employed to prevent a member government from enforcing its own laws against monopoly and restraint of trade (52). In the case of international services, it requires members to afford opportunities for direct consultation, instructs the ITO wherever possible to refer complaints to other intergovernmental agencies, and authorizes it, where no such agency exists, to make recommendations and promote agreement on remedies (53). The Organization is also empowered to conduct studies, make recommendations, and arrange for conferences on all matters relating to restrictive business practices in international trade (49).

CRITICISM AND APPRAISAL

Criticism of the chapter comes from two extremes. It is said, on the one hand, that it goes too far, limiting the freedom of domestic business to participate in foreign market-sharing schemes and subjecting it to both international and national control. It is argued that Americans cannot hope to sell in certain countries unless they agree to accept the quotas offered and observe the terms laid down by national cartels. It is feared that the *Charter* might be so interpreted as to circumscribe the activities of export trade associations organized under the provisions of the Webb-Pomerene Act. And it is contended that it is unfair to permit enforcement of the anti-trust laws while a case is under investigation or where a clean bill of health has been given by the ITO.

It is said, on the other hand, that the *Charter* does not go far enough, since it merely creates a forum for international discussion instead of outlawing cartels *per se*. It is pointed out that restrictive practices are to be judged, not by their form, but by their effects; that action on a case-by-case basis will be slow; that recommendations, in individual cases, will be passed upon, not by a judicial body, but by political appointees representing member states; that these

recommendations may be ignored; and that enforcement is left to national governments.

The fears of the first group of critics appear to be unjustified. If American exporters are satisfied with the terms accorded them by cartels that operate exclusively within the market of another country, it is unlikely that their participation will give rise to a complaint. If they are dissatisfied, however, the *Charter* affords means of taking action to free external competition in such markets from control. International agreements to divide up the world market, assigning certain countries to each participant as its exclusive territory, will certainly be condemned. But it cannot be contended that American business must enter into such arrangements in order to sell abroad. It is true that Webb-Pomerene associations are permitted to limit competition among their members, but as long as they compete with foreign sellers their activities should not be subject to complaint. They have never been authorized by Congress to participate in international cartels. Such participation might well give rise both to prosecution under the anti-trust laws and to investigation by the ITO. Its legality, under American legislation, is a matter for determination by the courts. Action under the *Charter* will not prevent the United States from enforcing the Sherman Act. Here the *Charter* is neutral: it does not amend the anti-trust laws; it does not interpret them.

The criticisms of the second group are not to be denied. But more is asked than is to be obtained. The *Charter* will not destroy monopoly in world markets overnight; the anti-trust laws have not destroyed it in the United States in sixty years. Restrictive business practices are to be judged by their effects; a rule of reason has governed the interpretation of the Sherman Act. Nations are not committed to take the action recommended in a given case; in the light of past traditions and present policies, their general commitment is stronger than anyone had reason to expect. Enforcement is left to governments; this will be the case as long as sovereignty is retained by national states.

The chapter marks the first approach toward international agreement in this field. Viewed as a beginning, it has great significance. The principle of competition in international markets is given formal

recognition. A common policy toward monopoly is established. Major commitments to action are taken. A forum is set up where restrictive business practices can be questioned and condemned. An instrument is fashioned through which corrective measures can be devised. A process of education is set in motion. A method is provided for accumulating a body of knowledge and experience. A foundation is laid for a structure of international common law to govern business practices in foreign trade. For the effective enforcement of its provisions, the pressure of world opinion must be brought to bear.

The Committee on Cartels and Monopoly of the Twentieth Century Fund closes its appraisal of the chapter with these words: "If the United States rejects the Draft *Charter*, it will get, not a better agreement, but a looser one, or perhaps no agreement at all. The right course for the United States is to support the adoption of the *Charter*, to adhere to it, and to try to improve it." *

* *Cartels or Competition?* (New York, 1948), p. 424.