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THE ROLE OF THE GRANGE IN THE ADVENT OF INDUSTRIAL REGULATION

By:
Winston W. Grant

**Department of Agricultural and Applied
Economics**

University of Minnesota
Institute of Agriculture, Forestry, and Home Economics
St. Paul, MN 55108

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Winston W. Grant*

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Winston W. Grant is Research Specialist and Extension Economist in
Legal Affairs, Department of Agricultural and Applied Economics,
University of Minnesota.

THE ROLE OF THE GRANGE IN THE ADVENT OF INDUSTRIAL REGULATION

I. INTRODUCTION

I want to discuss for you today the series of events by which the early Granges of Patrons of Husbandry left a really indelible mark on the business climate in which all American industry must function today. I am referring here to a broad segment of industrial regulation commonly referred to as antitrust law. Probably most people and even the lawyers and regulators who work with the anti-trust laws on a daily basis do not realize it, but it was the Patrons of Husbandry who initiated the Movement which eventually led to enactment of our first antitrust statute, the Sherman Antitrust Act of 1890.

So I want to begin by briefly reviewing some of the Granges' history, leading into development of the Agricultural Movement of the 1870's, enactment of the Sherman Act and how it backfired in the face of Agriculture. This, of course, led to enactment of exemptions for Agricultural Cooperatives from the antitrust laws. And finally, but perhaps most importantly, I want to talk about what has been happening with the Agricultural Cooperative Antitrust Exemption in the past few years—precisely, from 1973 through July of 1979.

II. SOME GRANGE HISTORY

There has apparently been some haggling over the years among some historians as to who should have credit as founder of the Grange, but it seems to me, if nobody here objects, that Oliver Hudson Kelly may be given the honor.

Oliver Hudson Kelly was just naturally a midwesterner and an agriculturalist, and I think we ought to claim him as a Minnesotan, but somehow he got himself born in Boston in 1826.[1] We really should not discredit Mr. Kelly for that because the same thing has happened to several of us Minnesotans and like the others of us, he got started in the right direction after he finished school by first moving to the midwest. In Chicago he worked as a drugstore clerk, then as a Tribune reporter. Then he moved to Peoria, Illinois and Bloomington, Iowa. But by the time he was 27 years old, Kelly was a well respected Itasca, Minnesota farmer and founding member of the Benton Agricultural Society.

Kelly's reputation in agriculture landed him a position with the USDA in 1864 and then he was selected as presidential inspector of post-Civil War southern agriculture. It was while he was on this inspection tour that Kelly conceived his plan for a National Agricultural Society to bring American farmers together in binding solidarity. The Grange was born in 1867 and the first official meeting was held by Potomac Grange #1, January 8, 1868 on 9th Street, Washington, D.C. So we cannot claim the first Grange, but we can claim the founder.

The original purpose of the Grange was social and educational but when Kelly went out into farm country to establish new Granges he had problems selling that concept to them. Remember that this was the post Civil War time and as is usually the case after a major war, American agriculture was in the throws of a depression. Agriculture was expanding at horrendous rates. For example, between

1860 and 1900 farmland increased from a little over 400 million acres to well over 800 million acres and the number of farms nearly tripled from 2 million to almost 6 million. Not surprisingly, agricultural markets could not begin to keep up with these huge increases in production, with the result that prices for agricultural products became very erratic but with the net result being terribly depressed agricultural prices. And along with the low prices came other detrimental economic pressures such as railroad tolls, high bank interest rates, expensive new implements to be purchased, grain storage fees, and depressed commodity prices.

While agriculture as a whole was growing tremendously, the individual farmer was but a powerless midget compared to the relatively huge firms who provided him with many of his services and supplies. The foremost of these were the railroad companies which were affecting the farmers very adversely with the hated railroad rebate system and a scheme of price discrimination between long and short hauls. The railroads and other large, economically powerful corporations like them came to be called monopolies and many of them later on adopted a business organization called the trust because of its taxation and other legal advantages. By the late 1880's there were trusts in sugar, whiskey, petroleum products, castor oil, coal, starch, and even salt and stoves.

So Oliver Kelly soon learned that it was not social and educational opportunities that would attract farmers to the Grange. As one author has put it, Kelly became firmly convinced that success of the Grange was tied to billing the Grange as an organization for the protection of the farmer against monopolies and

as a body committed to the economic improvement of its members. Consequently the main purpose of the Grange shifted at that time and farmers began to join the organization in droves.

The organization took two different approaches to help farmers with their plight. The first was to campaign against monopolies by seeking government control or regulation.[2] The second approach was to promote and build agricultural cooperatives with the hope that joined together in this way farmers could gain enough economic strength so as not to be at the mercy of the so called monopolists.[3]

Cooperatives began to grow, and the Grange with the support of many other farm organizations became very politically successful by getting state railroad regulation bills passed in many states. The Grange's role in getting this legislation passed was so important that the laws came to be known generally as the Granger Laws. Granger Laws were passed in Illinois, Ohio, Minnesota, Iowa and Wisconsin, most of the southern states and in several of the eastern states.[4] The Granger Laws stood up in the courts for over a decade until in 1886 they were struck down by the United States Supreme Court because they interfered with interstate commerce and as such were unconstitutional.[5]

III. THE FIRST FEDERAL INDUSTRIAL REGULATIONS ARE ENACTED: INTERSTATE COMMERCE ACT AND SHERMAN ANTITRUST ACT.

The move was on then for federal regulations and only a year later in 1887 the Interstate Commerce Act was passed and became the first real federal regulation of business establishing the first strong federal regulatory agency—the Interstate Commerce Commission.

Among other things, the Act outlawed the railroads' pools, rebates and short haul discrimination.[6]

Monopolies and trusts were still a problem. So the agricultural movement joined by labor and small business continued the antimonopoly movement which first gained success in the state legislatures. As before, however, the state laws did not work very well and the movement headed for Congress. Senator John Sherman of Ohio introduced the first federal antitrust bill to Congress in 1888. A year and a half later President Harrison signed the Sherman Antitrust Act on July 2, 1890.[7]

The battle had been a tough one but the movement had created such strong antimonopoly agitation that antitrust had been an important presidential campaign issue. The Grange and others had actually formed independent political parties called the Antimonopoly Parties in the midwest and monopolies were being referred to as "monster business establishments—dangerous to liberty." [8] The Sherman Act passed both Houses of Congress with only one dissenting vote.[9]

One part of the Sherman Act outlawed "every contract combination in the form of trust or otherwise or conspiracy in the restraint of trade." The second section of the Act made it a criminal offense to monopolize or attempt to monopolize any part of interstate commerce.[10] So in essence what the Act did was to try and outlaw all of the ways in which a firm could gain monopoly power and at the same time make it a criminal act for the firm to exercise monopoly power. In its most general terms, the courts have defined monopoly power as the power to fix prices and exclude competitors from the market.[11] So our first antitrust law was a very general one and one that a lot of people were not very happy with. As a matter of fact in the first years of

the Sherman Act the U. S. Attorney General would not even bring a case under the statute because he did not think the law was any good.[12]

The first real vigorous enforcement campaign came during the presidency of Theodore Roosevelt. During seven years of Roosevelt's Administration 54 court cases were initiated under the Sherman Act and Roosevelt became known as the "Trustbuster."[13]

After Roosevelt the Taft Administration initiated something like 90 antitrust proceedings. So we finally had federal antitrust enforcement in the United States which resulted in two very large and well known American corporations—namely Standard Oil of New Jersey and the American Tobacco Company—found to be illegal monopolies.[14]

IV. SHERMAN ACT BACKFIRES: COOPERATION ILLEGAL

But what about the American farmer? Were farmers getting the results they had sought? First of all was monopoly power being reigned in? And secondly were farmers able to build their economic strength through agricultural cooperation in order to counteract those economic giants which they were forced to deal with in the market place? Well, right off quick the answers to both of those questions are no! So the antimonopoly movement continued to thrive. The movement could not see that any real progress was being made in the control of monopoly power simply by charging a few corporations with monopolization. And secondly and very importantly for the purposes of our discussion, agricultural cooperatives, the farmers most important means for accumulating economic strength, were some

of the earliest and most hard hit targets under the Sherman Act.

The records of debates prior to enactment of the Sherman Act clearly indicate that sponsors of the bill certainly did not intend this result although it is equally clear that they may have anticipated it. Senator Sherman himself felt strongly enough about the issue that he proposed an amendment which would have provided very clearly that agricultural organizations or associations were not to be prohibited by the antitrust laws. But in the final analysis the agricultural exemption was dropped from the Sherman Act because it was generally felt that who would ever suppose that the federal antitrust law would be aimed at farmers.[15] Well they supposed wrong because under some of the early decisions the mere formation and therefore the mere existence of agricultural cooperatives was pronounced illegal.[16] So here we are with this great antitrust law which farmers in particular worked so hard for through the Grange and their other organizations for over twenty years and during the first fifteen years of the law's existence it has not done much of anything to control monopolies and it won't even let farmers form cooperatives.

To remedy this unhappy state of affairs the forces regrouped with the result being passage of the Clayton Act [17] in 1914. The Clayton Act amended the Sherman Act by extending application of the antitrust laws to acts and practices by business firms which might lead to lessening competition and restraining trade. In other words, the Clayton Act and also the Federal Trade Commission Act which was passed the same year were meant to "nip in the bud" situations

which had not yet resulted in monopoly but were quite likely to if left unchallenged. But quite importantly the Clayton Act provided the first specific exemption from the antitrust laws for agricultural associations—what we commonly call agricultural cooperatives, and it also, by the way, provided the exemption under which labor unions operate free from antitrust.[18]

The Clayton Act did not go quite far enough in its exemption for co-ops. Co-ops were still not allowed to incorporate and they could operate only for purposes of mutual self help. So farmer co-ops and especially milk co-ops continued to be harassed under the antitrust laws.

Well, the relentless troops had to regroup again and at this time they strove for solidarity by joining together the Cooperative Milk Producers Federation, The National Grange, The National Farmers Union, and other organizations to form the National Board of Farm Organizations. And for the first time farm co-ops established a unified voice at the source of their troubles in Washington D. C.[19]

This time the result was passage of the Capper-Volstead Act [20] of 1922 which had as its sole specific purpose the exemption of farmer co-ops from the antitrust laws. This exemption still places some restrictions on co-ops, for example, they must be operated for mutual benefit of the members, they must either restrict members to one man, one vote or limit dividends to 8 percent per year.

In section two, the Act gave the Secretary of Agriculture the authority to keep farmer co-ops from unduly enhancing their prices.

This 57 year old statute then, which has remained unchanged but not unchallenged, is the current state of federal statutory law under

which farm cooperatives must operate to avoid antitrust prosecution. Boiled down to its very basics this federal law provides that producers of agricultural products, including farmers, planters, ranchers, and dairymen, and nut and fruit growers may act together as corporations or not for the purposes of processing, preparing for market, handling and marketing and in the state and foreign commerce as long as they operate only for the mutual benefit of members and as long as each member has only one vote or the co-op does not pay more than 8 percent per year in dividends. And, of course, the co-op is not allowed unduly enhanced prices. What is meant by unduly enhanced prices is to this very day not settled on and it certainly is not an expression of great certainty. It is kind of like saying to the co-ops go ahead and process and market your products and charge whatever you want to but just be sure you do not charge too much. Farmers seem to have been quite happy with their state of affairs under the Capper-Volstead Act for almost 60 years. But now let's skip ahead 50 years or so to 1973 and see what other groups have had to say and do about the farmers antitrust exemption in the last six years.

V. WHAT HAS BEEN HAPPENING WITH CO-OP ANTITRUST EXEMPTIONS IN THE LAST FEW YEARS

It was in 1973 that various people, obviously not farming interests, began raising questions to whether cooperatives should remain exempted from the antitrust laws. These people seem to have noticed that cooperatives have grown in size and in number. That seems to be the central theme of most of the anti-cooperative debate these days—that cooperatives have gotten big, maybe too big, and that cooperatives have achieved market power and maybe too much market power. Certainly we all know

that cooperatives have become big and I don't think that anybody would argue that today's farmers have no market power. As a matter of fact, I took a quick look through the 1979 "Fortune 500" list of largest U.S. industrial corporations[21] and I found four agricultural cooperatives listed. One of these was our own Land O'Lakes with \$1.5 billion in annual sales.

So it is quite obvious that agricultural cooperatives have become big. But on the other hand, I only found four cooperatives in the "Fortune 500" which must mean there are 496 non-cooperative corporations among the largest. Agway, the largest agricultural cooperative of the "Fortune 500" ranked number 173. That means there are 172 corporations in America which are larger than the largest agricultural cooperative. So while agricultural cooperatives, or at least a few of them, have unquestionably become big businesses, they certainly do not pose a threat of takeover to the rest of the economy.

Nevertheless, over the past six years, we keep hearing questions such as: "Have cooperatives become too large?" "Are cooperatives gaining more than a countervailing power in their markets?" "Do cooperatives now have the power to monopolize, set unduly high prices for their products, and cause consumer food prices to rise too much?" These questions have been investigated by the United States Department of Justice, the Federal Trade Commission, and Congressional committees and the questions have been raised by consumer groups as well.[22] The Subcommittee on Monopolies and Commercial Law in the House of Representatives was one of the first groups to raise these issues back in 1973.[23] The focus of their attention was monopolistic practices and concentration on food industry. It's very difficult

these days to get very current economic data, but 1974-75 data indicate that all agricultural cooperatives in the United States as a group did less than \$56 billion worth of business.[24] That is a lot of sales, but if we take a look at the largest corporation in America in 1979, General Motors, that company alone did over \$63 billion worth of business.[25] So General Motors alone in 1979 did \$7 billion more business than all of the cooperatives did in 1974-75. If we take a look at the largest food company in America, Beatrice Foods, that company had sales in 1978 of \$6.3 billion.[26] That company alone did 1/10 as much business as all of the cooperatives combined.

As difficult as it is to come up with good data, I think it still can be concluded that farmers have not gained excessive market power through cooperation. Actually the Federal Trade Commission itself—one of the federal agencies which has been questioning agricultural co-ops—released a staff report in 1975 in which it concluded that "as a general rule, marketing cooperatives do not possess inordinate market power and are often completely overshadowed by corporations." [27] The FTC staff said that in such industries as grain and soybeans, livestock, cotton, tobacco and sugar "cooperatives do not play a major role although some regionals are able to actively compete with corporations." [28] However, the FTC staff did conclude that cooperatives dominate in the fruit, nut and milk industries. The report identified ten out of 490 fruit, nut and vegetable cooperatives which appeared to dominate certain commodity markets.

Some of the strongest statements yet concerning the market power of agricultural cooperatives have come from representatives of

the United States Department of Justice. In 1973 an assistant attorney general strongly urged that Congress should periodically review the cooperative exemption and suggested that "a 'super co-op' may....be able to raise prices to all processors who in turn have no alternative but to pass on higher prices to consumers." [29]

A Justice Department Staff Report on Milk Marketing in 1976 spoke strongly of "monopolistic control of the milk supply by dairy cooperatives" but the staff who wrote that report estimated that the cost of services rendered by milk cooperatives in 1973 added only less than 10¢ to the cost of one hundred pounds of milk. That's less than 1/10 of 1¢ per pound! The Justice Department staff also arrived at a figure of \$60 million which they labelled the social cost of cooperatives' monopolistic control of milk supply. [30] This figure sounds big in absolute terms but it has been questioned very seriously by other reputable economists. And if we look at that figure in relation to the total dairy products business volume of cooperatives in 1973-74, a total of \$7.2 billion, then the "social cost" is less than 9/10 of one percent of total business volume!

The latest group to take a shot at the cooperatives was the National Commission for Review of Antitrust Laws and Procedures. [31] This group was appointed in June of 1978 by President Carter. It was made up of officials of various administrative agencies, from Congress and one Federal Court judge. President Carter asked the Commission to look at two important areas. The first was these huge, complex antitrust cases which I am sure most of us have at least read about in the paper a few times which can stretch on for ten years or more and which can cost both parties to the case, whether it be private parties or the government, tens of millions

of dollars just for the investigation and legal expenses.

The other area of investigation, and the one that we are most interested in today, was existing exemptions from the antitrust laws and in this area the Commission looked into the antitrust exemption which co-ops have as a result of the Capper-Volstead Act. The Commission had a staff which made an investigation and then suggested several alternative recommendations which the Commission might make to the President.

Some of these alternative recommendations were rather harsh. For example, one staff option recommended that cooperatives be actually limited in terms of the number of members or in terms of total sales volume. Another was to limit the circumstances under which cooperatives could merge. A third option would have recommended that the second part of the Capper-Volstead Act which gave the Secretary of Agriculture the responsibility of not allowing cooperatives to increase prices too much, that is, to unduly enhance prices, should be taken away from the Secretary of Agriculture and be given over to the FTC, an agency which at best is not very friendly to farmers and particularly agricultural cooperatives.[32]

The second section of the Capper-Volstead Act seems to have become a real sore spot for those who have over the years questioned the agricultural exemption. Part of the problem appears to be the fact that for one reason or another no Secretary of Agriculture to date has ever instituted a legal action against an agricultural cooperative for charging unduly high prices.

In the final analysis, the Antitrust Commission made just two recommendations regarding the Capper-Volstead Act. In the first

place the Commission concluded that farmers should continue to be able to form cooperatives but that once cooperatives are formed their antitrust treatment should be similar to that of any other business corporation. The Commission would allow intercooperative agreements such as mergers only where competition is not substantially decreased. Finally the Commission recommended that section two of the Capper-Volstead Act should be amended to somehow define what is meant by undue price enhancement. In other words, the Commission would like the Capper-Volstead Act to say something about how much price increase is too much price increase.

Also, as a part of the second recommendation, the Commission recommended that the responsibility for enhancing this provision should be separated from promotional responsibilities of the U. S. Department of Agriculture.[34] Within the USDA there is a division which actually has the responsibility of helping cooperatives in promoting their goodwill and the Commission would like to see that this division does not also have the responsibility of being a cooperative watchdog. I suppose the Commission might feel that that situation would be similar to hiring a mouse to catch a cat rather than vice-versa.

This second recommendation was responded to rather quickly by the U. S. Department of Agriculture. Just this past July the USDA issued a detailed proposal for defining undue price enhancement and it proposed a new office within the Department to investigate, monitor, and where necessary, prosecute cooperatives for unduly enhancing prices.[35]

VI. CONCLUSION

In conclusion I think that as long as food prices continue to rise and draw public attention cooperatives will continue to be questioned as to whether or not their activities in the marketplace are contributing to those price rises. Consequently certain parties are going to continue to attack our agricultural antitrust exemptions. However, if successful, this recent USDA proposal concerning section two of the Capper-Volstead Act should at least appease many of the individuals in organizations who have for so long been upset by the possible conflict of interest and lack of enforcement of that statute.

To tie us back into the topic of the Granger's role, the Grangers work on behalf of American farmers. I recently read a report which indicated that the Grange is still at it by supporting legislation that would require companies which buy farm products to bargain in good faith with farmer cooperatives on commodity prices in terms of sale.[36] So even though the Grange is not as strong as it was at the height of its movement back in the 1880's it is still a good friend to American agriculture—after almost 113 years.

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