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Nebraska's Fair Trade Act

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Student Notes

NEBRASKA'S FAIR TRADE ACT

INTRODUCTION

Eighteen years ago the Nebraska Legislature enacted a Fair Trade Act[1] "to protect trade-mark owners, producers, wholesalers and the general public against injurious and uneconomic practices" in the distribution of trade-marked commodities. The Supreme Court of Nebraska recently found it necessary in *McGraw Electric Co. v. Lewis & Smith Drug Co.*,[2] to hold the act in violation of the constitution of Nebraska and the Sherman Anti-Trust Act.

The purpose of this article is to discuss and evaluate the *McGraw Electric* case with primary emphasis on the yardstick used by the court in determining unconstitutionality. The anti-trust issue will be discussed even though it is of minor importance since the particular holding of the *McGraw Electric* case in relation to anti-trust law is almost unique.

I. THE COURT'S YARDSTICK OF CONSTITUTIONALITY

In the *McGraw Electric* case, the plaintiff, an Illinois manufacturer and distributor of trade-marked toasters, signed retail price maintenance agreements with two Nebraska retailers pursuant to the Nebraska Fair Trade Act.[3] Defendant, a non-signer,[4] with knowledge of the agreements, advertised and offered for sale the trade-marked toasters at a price less than the minimum fixed by the agreements. Plaintiff sought an injunction and

1 Neb. Rev. Stat. §§ 59-1101 to 59-1108 (Reissue 1952).

2 159 Neb. 703, 68 N.W.2d 608, supplemental opinion, 160 Neb. 319 (1955). Companion case, General Electric Co. v. J.L. Brandeis & Sons, 139 Neb. 736, 68 N.W.2d 620 (1955).

3 Neb. Laws c. 136 (1937). The title of the act provides: "AN ACT to protect trade-mark owners, producers, wholesalers and the general public against injurious and uneconomic practices in the distribution of competitive commodities bearing a distinguishing trade-mark, brand or name through the use of voluntary contracts establishing minimum re-sale prices and providing for refusal to sell such commodities unless such minimum re-sale prices are observed. . . ."

4 Neb. Rev. Stat. § 59-1105 (Reissue 1952) provides: "Willfully and knowingly advertising, offering for sale or selling any commodity at less than the price stipulated in any contract entered into pursuant to the provisions of sections 59-1101 to 59-1108, 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."

damages. The trial court, denying the injunction, declared the act invalid. The Supreme Court of Nebraska affirmed on the grounds that, notwithstanding the validity of the act under the due process clause of the Fourteenth Amendment, it violated (1) the constitution of Nebraska in that it grants special privileges and immunities, deprives persons of liberty and property without due process of law, and confers upon persons the power to fix and enforce prices without imposition of standards; and (2) the Sherman Anti-Trust Act.

A. The Historical Basis of Fair Trade Legislation

In 1935 Illinois passed a Fair Trade Act which was similar in all material respects to Nebraska's present act. Seagrams Distillers Corporation, a wholesale dealer in alcoholic beverages, entered into retail price maintenance agreements with a number of Illinois retailers pursuant to the act. Old Dearborn Distributing Company, a non-signer, with knowledge of the agreements, sold the trade-marked beverages at a price less than the minimum fixed by the agreements. Seagrams sought an injunction against this violation of the Fair Trade Act. Old Dearborn defended on the grounds that the act denied due process of law and violated the equal protection clause of the Fourteenth Amendment. The United States Supreme Court, in *Old Dearborn Distributing Co. v. Seagrams Distillers Corp.*,[5] sustained the constitutionality of the act.

[5] 299 U.S. 183 (1936). The United States Supreme Court held that an owner of property cannot be denied the right to fix the price at which he will sell it, and that this "is an inherent attribute of the property itself, and as such within the protection of the Fifth and Fourteenth Amendments." Id. at 192. As to the nonsigner clause, the Court said: "The essence of the statutory violation . . . consists not in the bare disposition of the commodity, but in a forbidden use of the trade-mark, brand, or name in accomplishing such disposition. The primary aim of the law is to protect the property—namely, the good will—of the producer, which he still owns. The price restriction is adopted as an appropriate means to the perfectly legitimate end. and not as an end in itself." Id. at 193. The Court found that Fair Trade Acts do not fix prices, nor delegate power to private persons, but only permit certain persons to contract with regard to resale prices. The Court found no violation of due process since the acts were not unreasonable and arbitrary in their purpose of protecting the property right which the trade-mark owner has in his good will. The Court buttressed its decision on due process by adopting the concept that the retailers acquired the commodities with knowledge of the then existing price restrictions imposed by the resale agreements and by the statute, and that their voluntary acquisition of the property with such knowledge carried assent to the resale prices so known to be fixed. The Court also found the trade-mark owner's property right in his good will a reasonable basis for classification between trade-marked commodities and those not trade-marked, and consequently found no violation of equal protection of the laws.

Since *Old Dearborn,* there has been little doubt that fair trade legislation is constitutional within the meaning of the due process clause of the Federal Constitution. There is less harmony, however, in the application of *Old Dearborn* by the state courts to state constitutional provisions.[6]

For example, in *Old Dearborn,* the Court said:

> There is a great body of fact and opinion tending to show that price cutting by retail dealers is not only injurious to the good will and business of the producer and distributor of identified goods, but injurious to the general public as well. . . . True, there is evidence, opinion and argument to the contrary; but it does not concern us to determine where the weight lies. We need say no more than that the question may be regarded as fairly open to differences of opinion. The legislation here in question proceeds upon the former and not the latter view; *and the legislative determination in that respect, in the circumstances here disclosed, is conclusive as far as this court is concerned.* Where the question of what the facts establish is a fairly-debatable one, *we accept and carry into effect the opinion of the legislature.*[7] (Emphasis supplied)

The plaintiff in the *McGraw* decision argued that the *Old Dearborn* case sustained his contention that the Nebraska act was in the public interest and did not run afoul of constitutional prohibition. The Nebraska court, however, rejected this argument, and countered by using *Old Dearborn* as an authority for invalidating the act by saying:

> It is true that in the opinion there the court did arguendo in strong language indicate a conviction that such state legislation was constitutional.
>
> This however was not the issue decided by the United States Supreme Court. The issue decided there was that of whether or not the constitutionality of such legislation was a matter for determination by the state through its legislature and its courts or by the United States Supreme Court. It was held that this was a question for determination by and within the state, and

[6] See Grayson-Robinson Stores, Inc. v. Oneida Limited, 209 Ga. 613, 75 S.E.2d 161 (1953) (Georgia Fair Trade Act held violative of both the due process clause of the state constitution and the supremacy clause of the Federal Constitution); Shakespeare Co. v. Lippman's Tool Shop Sporting Goods Co., 334 Mich. 109, 54 N.W.2d 268 (1952) (Michigan Fair Trade Act held violative of the due process clause of the state constitution and an excessive exercise of the police power); Liquor Store, Inc. v. Continental Distilling Corp., 40 So.2d 371 (Fla. 1949) (Florida Fair Trade Act held an excessive exercise of the police power).

[7] 299 U.S. 183, 195 (1936).

in clear terms accepted the determination by the state on that basis.[8] (Emphasis supplied)

It would appear that the United States Supreme Court in *Old Dearborn* decided the only issue which was before it, namely, whether the Illinois Fair Trade Act contravened the due process and equal protection clauses of the Fourteenth Amendment. And it would appear from the language of the Court quoted above, that the same Court was deciding the issue of legislative versus judicial prerogatives rather than state versus federal prerogatives as assumed by the Nebraska court. For these reasons, it is submitted that the Nebraska court erred in their interpretation and application of *Old Dearborn,* the backbone of present day fair trade legislation.

B. Nebraska Standards of Constitutionality

In establishing a yardstick of constitutionality in the instant case, the Nebraska court relied heavily on its previous decisions in *Nelson v. Tilley*[9] and *Boomer v. Olsen.*[10] An analysis of these two cases, however, adds little to the perplexing problem of whether particular legislation is within constitutional limitations.

For example, the *Tilley* case concerned the validity of an act which regulated the licensing of motor vehicle dealers and the sale of motor vehicles.[11] Even though two minor subsections of the act were held to be invalid, the court upheld the remaining portions of the statute on the ground that the regulation was within the public interest and a valid exercise of the police power. The court said:

> Whatever the personal views of this court may be as to the necessity of such legislation, the fact remains that the legislature of the state concluded that a reasonable basis existed for its enactment and, there being some foundation in fact to justify legislative action, this court is powerless to substitute its judgment for that of the legislature, even if it cared to do so.[12]

However, it was held in the *McGraw Electric* case that the legislature had failed to express in the act "an indication of recognizable public interest"[13] and for this reason the court was

[8] McGraw Electric Co. v. Lewis & Smith Drug Co., 159 Neb. 703, 720, 68 N.W.2d 608, 617 (1955).

[9] 137 Neb. 327, 289 N.W. 388 (1939).

[10] 143 Neb. 579, 10 N.W.2d 507 (1943).

[11] Neb. Comp. Stat. §§ 60-901 to 60-919 (Supp. 1937).

[12] Nelson v. Tilley, 137 Neb. 327, 332, 289 N.W. 388, 392 (1939).

[13] McGraw Electric Co. v. Lewis & Smith Drug Co., 159 Neb. 703, 720 ,68 N.W.2d 608, 617 (1955).

"unable to find an escape from the conclusion that such a grant of power is unconstitutional and therefore void."[14] Since every possible presumption is in favor of the validity of a statute,[15] and since there can be little doubt that there was some reasonable foundation in fact to justify this legislation,[16] it would appear that the *Tilley* case strongly supports the plaintiff's contentions, yet the case was used almost exclusively to deny his contentions.

The *Olsen* case was the culmination of litigation concerning a statute which attempted to impose a maximum amount which employment agencies might charge their clients.[17] The statute was first attacked on the ground that the legislature was attempting to regulate a business not affected with a public interest.[18] The Nebraska court unanimously held that the statute was constitutional under the Nebraska constitution since employment agencies were affected with a public interest. However, the court felt compelled to strike down the statute as conflicting with the due process clause of the Fourteenth Amendment to the Constitution of the United States on the basis of *Ribnik v. McBride*,[19] which held that employment agencies were not affected with a public interest. Upon appeal to the Supreme Court of the United States the Nebraska decision was reversed and remanded on the grounds that the *Ribnik* case was no longer authority and that employment agencies were affected with a public interest.[20]

At this point the litigants had a unanimous decision by the Nebraska court that the statute was constitutional under the Nebraska constitution and a unanimous decision by the United States Supreme Court that the statute was constitutional under the Federal Constitution. The next step taken by the opponents of the statute was to institute a new state court action contending this time not that there was a lack of power in the legislature to fix maximum fees for employment agencies, but that the particular fee set in the statute was confiscatory. The opponents were at last victorious and the statute was held invalid under the Nebraska constitution since the provision fixing the maximum fees

14 Id. at 721, 68 N.W.2d 617.

15 Lincoln Federal Labor Union v. Northwestern Iron & Metal Co., 149 Neb. 507, 31 N.W.2d 477 (1948).

16 See quotation cited supra note 7.

17 Neb. Comp. Stat. § 48-508 (1929).

18 State ex rel. Western Reference & Bond Ass'n v. Kinney, 138 Neb. 574, 293 N.W. 393 (1940).

19 277 U.S. 350 (1928).

20 Olsen v. State of Nebraska ex rel. Western Reference & Bond Ass'n, 313 U.S. 236 (1941).

to be charged by such employment agencies was unreasonable, prohibitory and confiscatory. The court concluded the opinion by saying:

> We also hold that a private employment agency is not a business in which the public has such an interest that price fixing may properly be included as a method of regulation under the provisions of our Constitution.[21]

The court was confronted with an analogous situation in determining the validity of the Nebraska Unfair Sales Act,[22] which declared loss-leader sales unlawful. This act has been considered by the court in two cases, *State ex rel. English v. Ruback*,[23] and *Hill v. Kusy*.[24] In the *Ruback* case the plaintiff sought an injunction on the grounds that the defendant had sold coffee at less than cost in violation of the act. The defendant, among other things, argued that the act violated the due process clause since it tended "to fix prices in businesses not clothed with a public interest." In invalidating the act, the court said:

> The preliminary question now presented, in view of the essential nature of the transactions involved, is a mere sale of groceries, a transaction in no manner affected with a public interest.[25]

In the *Kusy* case, decided after the act had been amended, the plaintiff sought an injunction on the grounds that the defendant had sold cigarettes at less than cost in violation of the act. The defendant argued denial of due process. In this case the act was upheld, the court saying:

> In the exercise of and within the limits of its police power, the Legislature may forbid that which it deems to be an existing evil and it may limit its prohibitions to the matters which in its judgment menace the public welfare.[26]

It is to be noted with interest that the court in the latter case assumed that such business enterprises were affected with a public interest. It is difficult to understand why the sale of groceries in the first case is "in no manner affected with a public interest," whereas the sale of cigarettes some eleven years later in the second case is clothed with such a public interest that "the

[21] Boomer v. Olsen, 143 Neb. 579, 587, 10 N.W.2d 507, 511 (1943).
[22] Neb. Rev. Stat. §§ 59-1201 to 59-1206 (Reissue 1952).
[23] 135 Neb. 335, 281 N.W. 607 (1938).
[24] 150 Neb. 653, 35 N.W.2d 594 (1949).
[25] State ex rel. English v. Ruback, 135 Neb. 335, 340, 281 N.W. 607, 609 (1938).
[26] Hill v. Kusy, 150 Neb. 653, 657, 10 N.W.2d 594, 597 (1949).

Legislature may forbid that which it deems to be an existing evil."[27]

Whether it is possible to establish a workable yardstick of constitutionality is of course questionable. And it would appear that the only standard at the present time is that standard set forth in the *Tilley* case where the court said:

> The balance between due process and the police power is therefore more or less unstable, as it must necessarily keep pace with the economic and social orders.[28]

II. THE EFFECT OF THE MCGRAW DECISION ON FUTURE TRADE LEGISLATION

Other problems in the instant case are: (1) whether the end of the legislation is prohibited by the due process clause; and (2) whether the means authorized by the legislature violates the due process clause. In other words, does the *McGraw* decision prevent the legislature from imposing any type of control in future legislation, or does it merely prevent the legislature from using delegation to private parties to affect such controls.

It is difficult to determine from the opinion the answers to

[27] The Ruback and Kusy cases presented another aspect to the general problem of determining yardsticks. In the Ruback case the act was held invalid for vagueness because the elements of the conduct which the act attempted to define and punish were so vaguely expressed that the ordinary person could not determine in advance a course of lawful conduct. In the Kusy case, decided after the act had been amended, the act was upheld, the court holding that mere difficulty of application in the processes of litigation is not enough to enable a court to say that a statute is unconstitutional. It is difficult to reconcile these two cases on this point in view of Neb. Rev. Stat. § 59-1203 (Reissue 1952) which defines the violation as follows: "Sales at less than cost; advertising, when unlawful. It is hereby declared that any advertising, offer to sell or sale of any merchandise, either by retailers or wholesalers, at less than cost as defined in this act, with the intent, or effect, of inducing the purchase of other merchandise, or of unfairly diverting trade from a competitor, or otherwise injuring a competitor, impair (sic) and prevent (sic) competition, injure (sic) public welfare, and are (sic) unfair competition and contrary to public policy and the policy of this act, where the result of such advertising, offer or sale is to tend to deceive any purchaser or prospective purchaser, or substantially to lessen competition, or unreasonably to restrain trade, or to tend to create a monopoly, in any line of commerce." It would appear that this section is so vaguely expressed that the ordinary person could not determine in advance a course of lawful conduct, yet, the section was upheld as merely difficult of application. For an excellent article concerning the problems of "sales below cost," see Lovell, Sales Below Cost Prohibitions: Private Price Fixing Under State Law, 57 Yale L.J. 391 (1948).

[28] Nelson v. Tilley, 137 Neb. 327, 331, 289 N.W. 388, 392 (1939).

these important questions since the court discussed both ends[29] and means.[30] The inference which may be drawn from the court's discussion of unlawful means is that the end result, meaning some type of control, is lawful, since it can be argued that if the end control is unlawful, a discussion of the means to reach this unlawful end is unnecessary. That it is within the legislature's prerogative to enact some type of control is the reasonable inference to be drawn from the court's discussion; this inference is also supported by the fact that the court has approved of numerous controls of similar business enterprises.[31] It may be said, however, that the decision leaves these questions undecided and it is these questions which will concern legislators in drafting future trade legislation.

III. THE SHERMAN ANTI-TRUST ACT

Prior to *Old Dearborn*, states were hesitant to pass fair trade legislation since resale price maintenance agreements had been held violative of the Sherman Anti-Trust Act,[32] and there

[29] In discussing the issue of public interest in determining whether the legislation was within the police power, the court made the following statements: "It is impossible to draw from the act an indication of recognizable public interest to be served by the power which flows from section 59-1105. It is likewise impossible to draw any such indication from the title to the act." McGraw Electric Co. v. Lewis & Smith Drug Co., 159 Neb. 703, 720, 68 N.W.2d 608, 617 (1955). "It is trite to say that motive alone may not be accepted as a criterion for the determination of the constitutionality of legislative action.... The motive which induced the legislation does not and cannot become a check upon the power which is conferred by and inheres in the specific terms of the act." Id. at 720, 68 N.W.2d at 618.

[30] In discussing "means," the court said: "The question of whether or not legislation is in the public interest is ordinarily one for legislative determination, however it may not under the guise of regulation in the public interest impose conditions which are on their face unreasonable, arbitrary, discriminatory, or confiscatory." Id. at 720, 68 N.W.2d at 618. "There are no standards or requirements whereby contracting parties are obligated to conform to the claimed motivations or alleged purposes of the legislation.... Without any regard to these extraneously declared motives or purposes or any provision of the act, contracting parties may at will, with or without reason, arbitrarily, uncontrollably, or even capriciously by mere fiat and notice apply the provisions of section 59-1105." Id. at 721, 68 N.W.2d at 618.

[31] See Motors Acceptance Corp. v. McLain, 154 Neb. 354, 47 N.W.2d 919 (1951); Hill v. Kusy, 150 Neb. 653, 35 N.W.2d 594 (1949); Nelson v. Tilley, 137 Neb. 327, 289 N.W. 388 (1939).

[32] 26 Stat. 209 (1890), as amended, 15 U.S.C. § 1-7 (1952). Section 1 of the act provides: "Every contract, combination in the form of a trust or otherwise, or conspiracy, in restraint of trade or commerce among the several states ... is declared to be illegal...."

was widespread doubt about the constitutionality of such legislation. *Old Dearborn* established its constitutionality and brought on a flurry of legislative activity which included congressional enactment of the Miller-Tydings Amendment to the Sherman Act.[33] To alleviate the effect of two court decisions which later had drained the Fair Trade Acts of most of their vitality,[34] Congress passed the McGuire Act.[35]

The McGuire Act, which became law on July 14, 1952, eliminated the federal anti-trust obstacle from fair trade legislation by declaring that the enforcement of resale price maintenance agreements, against both signers and non-signers, shall not be declared unlawful under any federal anti-trust act in states where fair-trade legislation is authorized. The Nebraska court, however, found it necessary in the *McGraw* decision to hold expressly that the Nebraska act violated the Sherman Anti-Trust Act.

The reasoning to support this holding appears to be as follows: The Sherman Act, which declared contracts in restraint of trade in interstate commerce illegal, became law in 1890. The Nebraska act became law in 1937. The defendant argued that the Nebraska act was invalid at the time of its enactment since it was contrary to the Sherman Act as it then stood and was therefore repugnant to the supremacy clause of Article VI of the Constitution of the United States. The defendant further argued that since the act was invalid at the time of its enactment it continued to be invalid. Hence, the Miller-Tydings Amendment and the McGuire Act did not operate to validate the Nebraska act inasmuch as the act was void ab initio. In reply to this argument the Nebraska court said:

> In the Old Dearborn case it was pointed out substantially that though such state legislation as this was violative of the Sherman Anti-Trust Act it was not violative of the Constitution of the United States because thereof.[36]

[33] 26 Stat. 209 (1890), as amended, 15 U.S.C. § 1 (1952). The Miller-Tydings Amendment sanctioned resale price maintenance agreements in the fair trade states in transactions involving interstate commerce. This amendment was added as a proviso to section one of the Sherman Act.

[34] Schwegmann Bros. v. Calvert Distillers Corp., 341 U.S. 394, rehearing denied, 341 U.S. 956 (1951), and Sunbeam Corp. v. Wentling, 185 F.2d 903 (3d Cir. 1950), modified on rehearing, 192 F.2d 7 (3d Cir. 1951).

[35] 38 Stat. 719, (1914), as amended, 15 U.S.C. § 45 (1952). Act sustained in Schwegmann v. Eli Lilly Co., 205 F.2d 788 (5th Cir. 1953), cert. denied, 346 U.S. 856 (1953).

[36] McGraw Electric Co. v. Lewis & Smith Drug Co., 159 Neb 703, 712, 68 N.W.2d 608, 614 (1955).

It is interesting to note that the court did not expressly hold in the text of the opinion that the Nebraska Fair Trade Act was in violation of the Sherman Anti-Trust Act. However, the syllabus, which in Nebraska is prepared by the court and is to be taken as the true holding in the case, provides:

> The Fair Trade Act is not violative of the Constitution of the United States but is violative of the Sherman Anti-Trust Act.

Whether the court relied solely on *Old Dearborn* for this holding, or partially sustained the defendant's void ab initio argument, is not known. The reasonable inference to be drawn from the opinion is that the act was void ab initio since it was repugnant to the supreme federal law as it then stood. This would appear to be the only way to prevent application of the Miller-Tydings Amendment and the McGuire Act, which acts would operate to validate the Nebraska act on the anti-trust issue.[37] The holding is even more confusing in view of the statement in a leading Nebraska case where the court said:

> The section of an act properly amended should be construed precisely as though it had been originally enacted in its amended form.[38]

The courts of some twenty-six states have yet to pass on the validity of their fair trade laws. If the void ab initio argument discussed above is followed by these states, the acts passed prior to the Miller-Tydings Amendment would be totally void. Those acts passed subsequent to the Miller-Tydings Amendment but prior to the McGuire Act would be practically impotent for without the benefit of the McGuire Act and the non-signers clause, the acts would not be enforceable. This result could hardly have been the intention of Congress in passing the Miller-Tydings Amendment and the McGuire Act. To this date, only one other court has used similar reasoning in invalidating their Fair Trade Act.[39]

IV. CONCLUSION

From the foregoing it is evident that the yardstick of constitutionality used by the court is extremely difficult, if not im-

[37] It is also interesting to note that neither the Miller-Tydings Amendment nor the McGuire Act were cited or referred to in the opinion of the instant case.

[38] First Trust Co. v. Smith, 134 Neb. 84, 91, 277 N.W. 762 767 (1938).

[39] Grayson-Robinson Stores, Inc. v. Oneida Limited, 209 Ga. 613, 75 S.E.2d 161 (1953).

possible, to ascertain. The instant case adds little to the establishment of such a standard. And it is submitted that the real issue in the *McGraw* decision was the long standing controversy concerning the scope of legislative and judicial prerogatives. That this controversy will continue to produce unstable results can hardly be doubted. Yet it would seem, in the absence of workable standards, that the court, in deciding such controversial issues as raised in the instant case, would allow the opinion of the legislature to stand.[40]

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