

JUDICIAL TOLERANCE OF FARMERS' COOPERATIVES*

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A decade and a half of judicial tolerance has been ended by a decision of the United States Supreme Court unfavorable to farmers' cooperative associations.¹ A legislative act declaring the ginning of cotton to be a "public business" has been made to invalidate another act of the same legislature providing for the granting of permits to gin to cooperatives upon the petition of "one hundred citizens and taxpayers of the community." It is held by the Court that since the business is public, it cannot be entered without a license; that in form and purpose the association is a corporation; and that the legislative prescription of different conditions to individuals and "corporations" as a requisite for licenses is a denial of "the equal protection of the law" guaranteed by the Fourteenth Amendment. The judgment of the Court is alike of immediate import and of future significance; it necessitates the revision of tactics now employed in the conduct of cooperative associations; it may well lead to basic changes in the prevailing form of the organization or seriously retard the advance of the movement. An understanding of the meaning and import of the rule of law implicit in the decision demands a brief account of the ends, the forms, and the legal status of the cooperative association.

The cooperative represents an attempt of the farmer to adjust himself to the ways of modern business. He is by trade, by habit, and by tradition a producer rather than a bargainer, a husbandman rather than a trader. The necessity of taking his product to market, exacting the best price he can get, and purchasing a living has been forced upon him by the march of unwilling events. The older America, save for a dotting of towns and an occasional city, was made up of quite-like, almost self-sufficient, all-but-isolated farms. What was consumed by the household was for the most part raised on the place; whether a family was well or poorly off depended primarily upon hard work, skill, foresight, and the favor of the seasons; the family living was for the most part made rather than bought. But "science," the machine, and engineering converted an aggregation of small, homogeneous, industrial units into a great and

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¹ Frost v. Corporation Commissioners, 49 Sup. Ct. 235 (U. S. 1929).

interlocking industrial system. Since a more efficient farming demanded less labor, a surplus population left the farms for the city; since up-to-date agriculture gave a larger yield, surplus crops had to be marketed. Thus unwittingly the farmer who had been the bulwark of the agricultural regime was dragged into the commercial system; he came to produce "cash crops," to take his pay in "money," and to "buy the goods" on which his family lived. Whether or no, he was converted into a "business man."

But, from the first, the farmer has viewed with suspicion and hostility "the business game." By his universal confession he has played it as a blundering amateur. With him, unlike merchant and manufacturer, bargaining is recurrent rather than habitual; "for three hundred and sixty days in the year the farmer has been a producer . . . then for a few days he suddenly becomes a trader."² The persons who are gainfully employed in agriculture are many, widely scattered, and personally unacquainted with each other. The seller of cotton or wheat or fruits, skilled as he may be in petty dickering with a neighbor or a stranger, has a feeling of impotence in facing alone "the market" and attempting through intermediaries to negotiate with the unseen and unknown purchasers of his products. The ordinary farmer must sell when his crop is ready; he has neither cash nor storage to enable him to await a more favorable season. Nor has he the technical knowledge or the skill in forecasting to enable him to anticipate a favorable turn of the market. It is his ill luck that he takes the fruits of his labor to market just when his neighbors are taking theirs. It may be, of course, that the farmer is relatively well off, that the ills of which he complains are only those of other men or largely imaginary. It is probably true that no small part of them are due to an uncontrolled production which floods the market with surplus supply and depresses price. But the market is the point at which he comes into contact with the outside world and takes the shock. He knows, or thinks he knows, soils, crops, processes, and even the weather; but to him the increase and decrease in demand and the capricious ups-and-downs in price, the many conditions and causes of which lie at the ends of the earth, are veiled mysteries.³ He meets these "forces," which bountifully give or stingily withhold the good things of life, in the persons of those

² Meyer, *The Law of Cooperative Marketing* (1927) 15 CALIF. L. REV. 85, 94.

³ With respect to the law of supply and demand, one writer has said "The farmers . . . found the movable factors in that law—time and place; and they learned that the most important element in making price was . . . the ability to adjust supply to demand at any given time and place." Sapiro, *The Law of Co-operative Marketing Associations* (1926) 15 KY. L. J. 1, 2.

with whom he bargains in the disposition of his crops. So the deficit between expectations and gains is due to middlemen, to the enormous costs which distribution eats up, to the perniciousness or the inefficiency of the system of marketing.⁴ To the market, then, his troubles are due; to banish them, a new marketing system must be devised.

The attempt to hit upon a constructive solution of the marketing problem presents a long chapter in trial and error the end of which is not yet. If the farmers were to control, rather than to be controlled by, their market, a scheme for concerted action was necessary. A voluntary association was far too unstable and a business corporation far too alien to meet the needs of the community enterprise. It was essential to contrive a new type of "business unit" which would make easy the relations between association and members, give stability to the venture, and preserve its character as a "mutual benefit society." It chanced that several decades ago a group of consumers in an English town, intent upon protecting themselves against "the wastes" and the "extortions" of "middlemen" had banded themselves into a cooperative. The Rochdale scheme,⁵ invented by a party on the other side of the market, was borrowed as the germ of the new agricultural organization. But urban England is not rural America, the needs of buyers are not those of sellers, and the acquisition of household necessities is not the disposition of staple crops; so the buyers' cooperative had to be converted into an institution which would serve the needs of producers.⁶ For many years there has been experimentation in selecting, borrowing, adapting, contriving and fitting together devices, procedures, and arrangements into an organization that will meet passably well the peculiar demands upon it. In this process many elements of the business corporation have been adapted to the requirements of the cooperative venture. A current survey reveals great variety in the structure of the organization; a historical account points towards the emergence of a form which in outward appearance is a business corporation and in

⁴ "When the World War ended . . . for the producers of agricultural products the prices were low, and there was no profit. To the consumer prices were so high that consumption was restricted. . . . Middlemen, speculators, and people who stood between the producers and consumers derived excessive profits from this situation, while the producers and laborers were denied a living. . . ." Clark, C. J. in *Tobacco Growers Co-op. Ass'n v. Jones*, 185 N. C. 265, 276, 117 S. E. 174, 179 (1923).

⁵ FAY, *COOPERATION AT HOME AND ABROAD* (1925).

⁶ The cooperative movement has been judicially termed "the most hopeful movement ever inaugurated to obtain justice for and improve the financial condition of farmers and laborers." *Tobacco Growers' Co-op. Ass'n v. Jones*, *supra* note 4, at 277, 117 S. E. at 179. An estimate places the number of cooperatives in existence in this country at 12,000 with a membership of 2,700,000.

end a mutual benefit society.⁷ But the accommodation of structure to function is not yet complete.

In its attempt to find the proper form and to command support, the cooperative association has not had easy going. A morale has not been easy to maintain among scattered and independent farmers; loyal supporters in days of their own need have been prone to break away when on occasion outside buyers were offering better prices; from the "inside" success has been constantly impeded by "forces" tending "to undermine the vital confidence and spirit of members."⁸ From the outside the cooperative has had to contend against the opposition of parties who have vested interests in the established institutions. If in time this form of association is to displace other marketing agencies, or to take a high place among them, it must be upon its proven merits. The legislature, by recognizing its peculiar form and approving its specific practices, can only accord it a chance of success in competition with rival organizations. The courts, a more delicate agency of control, can do no more than make a detailed accommodation of the law of the land to the exigencies of a developing type of organization.

Almost from the first the farmers' cooperative has been looked upon with favor by the legislature. This has been due in part to practical politics; the farmers are numerous and have votes and their representatives are not unmoved by political considerations. In part it rests upon a deeply seated conviction of "the unequal bargaining power of the agricultural class" in disposing of its products and a feeling that an association of farmers is not likely to be so comprehensive or so coercive as to threaten monopoly.⁹ In a series of acts Congress has exempted farmers' cooperatives from the income tax,¹⁰ given them an immunity from the federal anti-trust statutes,¹¹ and established

⁷ A detailed history of the cooperative movement, of the forms which cooperative marketing has taken, and of the reason for its rapid growth is to be found in STEEN, *COOPERATIVE MARKETING* (1923).

⁸ It is beyond the scope of this article to describe these inside methods. They are briefly and clearly explained by Sapiro, *op. cit. supra* note 3.

⁹ "There was no intention . . . to enable the producers to combine to sell their products at a profit beyond what would be a fair and reasonable market price. Indeed, this would be impossible . . . as only a part of them would in any event belong to such an organization; whereas the manufacture of tobacco, being in comparatively a few hands, the buyers could combine as they have done for many years, in a so-called 'gentlemen's agreement' to fix the price. . . ." Clark, C. J. in *Tobacco Growers Co-op. Ass'n v. Jones*, *supra* note 4, at 272-273, 117 S. E. at 177.

¹⁰ Revenue Act of 1926, § 231 (12), 44 STAT. 40 (1926), 26 U. S. C. § 982 (1926).

¹¹ Section 6 of the Clayton Act, 38 STAT. 730 (1914), 15 U. S. C. § 17 (1926) exempted agricultural associations "for the purpose of mutual help and not having capital stock"; this having been found unsatisfactory, as too

a bureau in the Department of Agriculture to aid in their development.¹² With a surprising unanimity in end, if with a great variety in language, the legislatures of many states have conferred upon the associations such favors as the enforcement of membership contracts by injunction, the recovery of liquidated damages for breaches of contracts by a member, a protection of contracts by appropriate penalties against interference from without, and immunity from prosecution under state anti-trust laws.¹³ All in all more than forty states¹⁴ have now adopted, with slight variations, the so-called Cooperative Marketing Act.¹⁵

Nor have the courts been slow to follow where the legislature has led. The story of the development of the law of cooperative marketing has been set forth in clear-cut perspective and with colorful detail and cannot be repeated here.¹⁶ It is enough to say that the cases disclose a vast array of judicial utterance monotonous alike in judgment and in dicta. Almost without exception the opinions begin with a review of the oppressive conditions with which the agricultural class is beset, discover cooperative marketing to be an appropriate means of relief, and conclude that the particular legislative proviso or cooperative practice which is in question in the case is a proper and valid means for promoting the larger end. It seems obvious that if cooperation is to be effective it must involve some departure from competition, exhibit some tendency towards monopoly,¹⁷

limited, the Capper-Volstead Act, 42 STAT. 388 (1922), 7 U. S. C. c. 12 (1926), included in the exemption organizations "with or without capital stock."

¹² Cooperative Marketing Act, 44 STAT. 802 (1926), 7 U. S. C. c. 18 (1926). See also an act "to prevent discrimination against cooperative associations," 44 STAT. 1423 (1927). For comment on this federal legislation, see NOURSE, *THE LEGAL STATUS OF AGRICULTURAL COOPERATION* (1927) c. XI.

¹³ "In the space of five years, the legislatures and courts have made greater progress in clarifying the rights, powers, and obligations of cooperatives and their members than was accomplished in the first generation of ordinary corporation development. This is a tribute . . . to the hope that in cooperative marketing may be found a partial solution of the difficulties that beset the farmer." Sapiro, *op. cit. supra* note 3, at 20.

¹⁴ Delaware alone is still entirely without statutory provision for the creation of farmers' cooperatives. Vermont provides for them only by a section in her general corporation law.

¹⁵ This model enabling legislation was drawn by Mr. Aaron Sapiro. For an excellent discussion of the legal status of these acts as passed by the various states, see Tobriner, *The Constitutionality of Cooperative Marketing Statutes* (1928) 17 CALIF. L. REV. 19. A typical example of this legislation is the Bingham Cooperative Marketing Act of Kentucky. Ky. Acts 1922, c. 1.

¹⁶ See NOURSE, *op. cit. supra* note 12. See also a report to the Senate by the Federal Trade Commission on Cooperative Marketing (1928).

¹⁷ With reference to this feature, a writer has said: "The issue is one which may be faced frankly. The commodity plan does contemplate com-

and run some risk of being held to be "in restraint of trade." This serious hazard, which might well have resulted in a paralysis of the movement, has been almost removed.¹⁸ Although in one state the threat remained as late as 1925, it seems clear that cooperative associations are now immune from challenge as being in themselves in restraint of trade.¹⁹ Although at first the courts were disposed to regard the special remedies, exceptions, and immunities conferred upon cooperatives by the legislature as unfair classification in violation of the Fourteenth Amendment,²⁰ it has of late been repeatedly held that such provisions are well within the discretion of the law-making body.²¹ Quite without exception the highest state courts have sustained the

modity control, and it often leads directly into monopoly. The sooner that is generally understood, the better off co-operatives will be." Steen, *op. cit. supra* note 7, at 306.

¹⁸ Atkinson v. Colorado Wheat Growers' Ass'n, 77 Colo. 559, 238 Pac. 1117 (1925). Other leading cases showing the early unfavorable attitude of the courts on this issue are: Ford v. Chicago Milk Shippers' Ass'n, 155 Ill. 166, 39 N. E. 651 (1895); Reeves v. Decorah Farmers' Co-op. Society, 160 Iowa 194, 140 N. W. 844 (1913); Georgia Fruit Exchange v. Turnipseed, 9 Ala. App. 123, 62 So. 542 (1913); Burns v. Wray Farmers' Grain Co., 65 Colo. 425, 176 Pac. 487 (1918).

¹⁹ Meyer, *op. cit. supra* note 2, at 93; Dark Tobacco Growers' Co-op. Ass'n v. Dunn, 150 Tenn. 614, 266 S. W. 308 (1924); Potter v. Dark Tobacco Growers' Co-op. Ass'n, 201 Ky. 441, 257 S. W. 33 (1923); List v. Burley Tobacco Growers' Co-op. Ass'n, 114 Ohio 361, 151 N. E. 471 (1926); Liberty Warehouse Co. v. Burley Tobacco Growers' Co-op. Marketing Ass'n, 276 U. S. 71, 48 Sup. Ct. 291 (1928). Indicative of the change of attitude on the issue of restraint of trade are the words of the Minnesota court: "Subsequent to the World War . . . [the farmer's] condition was critical. The state, and in fact the government, responded to a sympathetic cooperation in an economic rehabilitation of the stability of the agricultural interest. The policy of our nation is apparent in exempting agricultural organizations, instituted for the purpose of mutual help . . . from the operation of the Sherman Act." Minn. Wheat Growers' Co-op. Ass'n v. Huggins, 162 Minn. 471, 475, 203 N. W. 420, 422 (1925).

²⁰ The general attitude of the early decisions is expressed by the Supreme Court in the case of Union Sewer Pipe Co. v. Connolly, 184 U. S. 540, 563, 22 Sup. Ct. 431, 441 (1902): "If combinations of capital, skill, or acts . . . are hurtful to the public interests and should be suppressed, it is impossible to perceive why like combination in respect of agricultural products and livestock are not hurtful." And a lower federal court speaks to the same effect: "We are familiar with the duties of the farmer and the cares and trials of his business life, and appreciate highly the customary compliments paid by mankind to the rural yeomanry of the land . . . yet what is there about all that to entitle him to the privilege of combining in restraint of trade . . . while . . . the storekeeper and mechanic are precluded therefrom." *In re Grice*, 79 Fed. 627, 649 (C. C. N. D. Tex. 1897).

²¹ N. Wisconsin Co-op. Tobacco Pool v. Bekkedal, 182 Wis. 571, 197 N. W. 936 (1923); Oregon Growers' Co-op. Ass'n v. Lentz, 107 Ore. 561, 212 Pac. 811 (1923); Clear Lake Co-op. Livestock Shipper's Ass'n v. Weir, 200 Iowa 1293, 206 N. W. 297 (1925); Harrell v. Cane Growers' Co-op. Ass'n, 160 Ga. 30, 126 S. E. 531 (1925).

validity of the standard Cooperative Marketing Act;²² and, through Mr. Justice McReynolds, speaking for the full bench, the United States Supreme Court has declared that "cooperative marketing statutes promote the common interest."²³

Nor has a series of favorable decisions often been interrupted by an adverse judgment. A detailed search for overt practices which have been put under the judicial ban yields scanty results. In fact, earlier decisions and inconsequential points aside, one is driven largely to dicta for verbal evidence of an unfavorable attitude. "Secondary boycotts" are not to be permitted.²⁴ It would be as much as its existence was worth for it to be proved that a cooperative had been formed for the sole purpose of manipulating the market;²⁵ even the fixing of an "unduly" high price might constitute an adequate reason for its dissolution.²⁶ "Educational work" aiming at a restriction of production has been held legal;²⁷ but a threat of invalidity has been uttered against covenants among members to grow or not to grow a given crop at the discretion of the association.²⁸ A trio of recent decisions insist that a strict compliance with statutory provisions is a condition essential to the enjoyment of exceptional privileges.²⁹ But such instances of disapproval and admonition indicate at most that there are limits of tolerance beyond which the cooperatives will not be permitted to go.³⁰

²² A few leading cases in addition to those cited above are: *Warren v. Alabama Farm Bureau Cotton Ass'n*, 213 Ala. 61, 104 So. 264 (1925); *Tobacco Growers' Co-op. Ass'n v. Jones*, *supra*, note 4; *Rifle Potato Growers' Co-op. Ass'n v. Smith*, 78 Colo. 171, 240 Pac. 937 (1925).

²³ *Liberty Warehouse Co. v. Burley Tobacco Growers' Cooperative Marketing Ass'n*, *supra* note 19.

²⁴ *United States v. King*, 250 Fed. 908 (D. Mass. 1916).

²⁵ *People v. Milk Exchange*, 145 N. Y. 267, 39 N. E. 1062 (1895).

²⁶ See *Owen County Burley Tobacco Society v. Brumback*, 128 Ky. 137, 107 S. W. 710 (1908); *Dark Tobacco Growers' Co-op. Ass'n v. Mason*, 150 Tenn. 228, 263 S. W. 60 (1924).

²⁷ *List v. Burley Tobacco Growers' Co-op. Ass'n*, *supra* note 19. The tendency towards limiting the supply occurs more naturally in the commodities, such as fruits or nuts, which require a long period of culture before being ready for marketing.

²⁸ Keegan, *Power of Agricultural Co-operative Associations to Limit Production* (1928) 26 MICH. L. REV. 648.

²⁹ *Fisher v. El Paso Egg Producers' Ass'n*, 278 S. W. 262 (Tex. 1925) (association held in restraint of trade, having operated for a year without attempt to come under the provisions of the state enabling act); *American Livestock Commission Co. v. United States*, 28 F. (2d) 63 (D. Okla. 1928) (cooperative not entitled to seek relief against boycott by market agencies at stockyards, since not authorized to handle products of non-members); *McCauley v. Arkansas Rice Growers' Co-op. Ass'n*, 171 Ark. 1155, 287 S. W. 419 (1926) (purchase of rice for profit by association held violation of contract with members as beyond scope of power).

³⁰ For example, in *Minn. Wheat Growers' Co-op. Marketing Ass'n v.*

It is against such a background and into a smoothly running course of judicial approval that the unfavorable judgment in the *Frost* case is projected. The case presents in epitome the whole problem of the structure and function of the cooperative association and of its legal control. The question before the Court was a complex one; the issues discussed were numerous and badly tangled. The opinions are so grounded in the circumstances out of which the litigation grew that they are well nigh meaningless apart from a detailed knowledge of the facts.

The beginning of the matter lies in a chapter of the legislative history of Oklahoma. It goes back nearly twenty years, to the days of "the new freedom" and "the new nationalism," to "the spirit of 1912," and the general belief that great political and industrial ills were to be cured by legislation. The good people of Oklahoma were not immune to the general dissatisfaction so prevalent throughout the cotton belt at the opening of the World War. To satisfy their demands, even if not to relieve their distress, two comprehensive statutes were passed by the legislature. The act of 1915 declared the ginning of cotton to be a "public business,"³¹ to be carried on only under a license from the Corporation Commission. To those already engaged permits were to be given as a matter of course, but licenses for new gins were to issue only upon a showing of public necessity. This was to be

Huggins, *supra* note 19, at 477, 203 N. W. 420 at 423: "We do not say that this organization like any other corporation, association, or individual may not violate the law. It may. If so, it may be punished the same as all others . . . who transgress." And to similar effect is the following from the Alabama court: "If it should in the future appear . . . that this association is being used for unlawful purposes to the injury of the public interest, by creating a scarcity of cotton or by unreasonably enhancing its market price, it will be the proper function of a court of equity to grant relief accordingly." *Warren v. Alabama Farm Bureau Cotton Ass'n*, *supra* note 22, at 66, 104 So. at 269. See also *List v. Burley Tobacco Growers' Co-op. Ass'n*, *supra* note 19; *Washington Cranberry Growers' Ass'n v. Moore*, 117 Wash. 430, 201 Pac. 773 (1921). It has been suggested that "the courts have been so swayed by emotions of sympathy with the farmer" as at times to compromise "the stricter form of judicial reasoning." *NOURSE, op. cit. supra* note 12, at 428.

³¹ It is significant that the term employed is "public business," not "public utility" or business "affected with a public interest." It is doubtless true that at the time the ginning business was being overdone, and there was a demand for fewer and better gins. The act did provide for a regulation of charges; but there is no evidence to show that the legislature was willing to give up such protection as competition afforded the patrons of gins for a dubious trial at authoritative price regulation. On the contrary their intent was probably to make assurance half way sure by trying both methods. It is manifest that there is nothing inconsistent between licensing gins only upon a showing of necessity and a maintenance of competition between them. In short the term "public business" serves admirably when the intent is both to keep competition and to attempt price regulation.

attested by "the presentation of a petition signed by no less than fifty farmer petitioners of the immediate vicinity."³² The enabling act of 1917 made provision for the formation by persons engaged in agriculture or horticulture of cooperative associations without capital stock and not conducted for profit.³³ In 1919 this was amended to permit the formation of "corporations" with capital stock, but under legislative limitations designed to preserve their features of "mutual benefit" and their cooperative character.³⁴ In 1923 "the petition of fifty farmer petitioners" was struck from the cotton ginning act as the test of public necessity,³⁵ and in 1925 there was inserted in lieu of it the proviso, "that on the presentation of a petition for the establishment of a gin to be run cooperatively, signed by one hundred citizens and taxpayers of the community where the gin is to be located, the Corporation Commission shall issue a license for said gin."³⁶

It is with the validity of these statutes and the rights under them that the case is concerned. Frost owned a ginning business in Durant; whether he was so engaged in 1915, or whether he secured his permit by a proper showing of "public necessity," the record does not disclose. The Durant Cooperative Gin Company was organized under the act of 1917 as amended in 1919; it presented to the Commission a petition signed by "one hundred citizens and taxpayers" and asked for a license to establish a gin in Durant. Frost protested in writing that there was no "public necessity" for an additional gin. The Commission, holding the proviso relative to cooperative associations mandatory, refused to heed his request. Frost, alleging "the proviso" to be in violation of the "due process" and "the equal protection of the laws" clauses of the Fourteenth Amendment, brought suit for an injunction restraining the Commission from issuing the license. After a number of preliminary steps,³⁷ the federal district court denied the prayer for relief.³⁸ Upon appeal by Frost, the United States Supreme Court has reversed this judgment. The opinion of the court was delivered by Mr. Justice Sutherland; there were vigorous dissents by Mr. Justice Brandeis and

³² Okla. Laws 1915, c. 176, OKLA. COMP. STAT. (1921) §§ 3712-3718.

³³ *Ibid.* § 5599.

³⁴ *Ibid.* § 5637 *et seq.*

³⁵ Okla. Laws 1923, c. 191, OKLA. COMP. STAT. (Supp. 1926) § 3713.

³⁶ Okla. Laws 1925, c. 109, OKLA. COMP. STAT. (Supp. 1926) § 3714.

³⁷ It is hardly necessary here to present in detail the course of the litigation. A history of it is given in the dissenting opinion of Mr. Justice Brandeis, *Frost v. Corporation Commission*, *supra* note 1, at 240-241. It is enough to note that a preliminary question was passed upon by the U. S. Supreme Court. *Frost v. Corporation Commission*, 274 U. S. 719, 47 Sup. Ct. 589 (1927).

³⁸ *Frost v. Corporation Commission*, 26 F. (2d) 508 (W. D. Okla. 1927).

Mr. Justice Stone, in both of which Mr. Justice Holmes joined. The opinion of the Court falls into two very distinct parts. The first, an offensive argument, is that "the proviso" which permits "corporations" to obtain licenses upon terms less exacting than those prescribed for individuals is a denial of "the equal protection of the laws." The second, a defensive argument, is that there is no escape by way of proper legislative discretion, because cooperatives organized as business corporations are not valid subjects of classification. Each of these has its distinct significance for the cooperative movement.

The argument by which the positive case is made out can be very briefly stated. In Oklahoma the ginning of cotton is by legislative act a "public business," to be engaged in only under a "permit" which is to issue only after "a showing is made that such a plant is a needed utility." "It follows that the right to operate a gin and to collect tolls therefore . . . is not a mere license, but a franchise." It is "a right, privilege, or power which by every legitimate test is a franchise."³⁹ "The right . . . is . . . exclusive against any person attempting to operate a gin without a permit . . . or against one who attempts to do so under a void permit." In either case "the owner may resort to a court of equity" for protection against "an injurious invasion of his property rights." The license given to the Durant Cooperative Company is "void"; it was obtained under "a proviso" which is a "nullity"; because under it "a greater burden" is laid upon "an individual" who wishes to engage in the ginning of cotton than upon a cooperative association. Thus "the proviso" is a denial of "the equal protection of the laws" guaranteed by the Fourteenth Amendment.⁴⁰

The mere statement of the simple lines of this argument reveals the many difficulties with which it is beset. Like the minority of the court, many careful students will find themselves sorely puzzled by the course of the reasoning. In the words of the Oklahoma statute the ginning of cotton is declared to be a "public business," not a "public utility"; in the language of the legislature and of the state courts,⁴¹ a "license" is only a license. It is true that in general public service industries are carried on under franchise.⁴² But if a "license" is a "franchise" in such

³⁹ It is manifest that, although Mr. Justice Sutherland is using the vocabulary, his argument does not run in terms of the Hohfeld system.

⁴⁰ *Frost v. Corporation Commission*, *supra* note 1, at 237-238.

⁴¹ *Choctaw Cotton Oil Co. v. Corporation Commission*, 121 Okla. 51, 247 Pac. 390 (1926).

⁴² To support the argument that in a "public business" a license is a franchise, Mr. Justice Sutherland cites: *Walla Walla v. Walla Walla Water Co.*, 172 U. S. 1, 19 Sup. Ct. 77 (1898); *California v. Central Pacific R. R.*, 127 U. S. 1, 8 Sup. Ct. 1073 (1888); *Monongahela Navigation Co. v. United States*, 148 U. S. 312, 13 Sup. Ct. 622 (1893); *Owensboro v. Cum-*

businesses as transportation, the supply of water, and the provision of telephone service, which are monopolistic in character, make use of public property, and are endowed with the right of eminent domain, it does not follow that a license is a franchise in the business of cotton ginning which is competitive in character, uses no public property, and is not endowed with the right of eminent domain.⁴³ Even if it be admitted that the license is a franchise, it does not follow that it is exclusive, that the right which it confers is to be interpreted as a denial of a like right to another, or that the legislature may not modify or take away a "property" right which is of its own creation.⁴⁴ The positions taken by Mr. Justice Sutherland are not without legal support; but it is significant that every one of the debatable issues has to be resolved in Frost's favor, or else his cause fails.

Nor are the difficulties resolved by an attempt to discover the source of the property right which is threatened by a license for a new gin. The ordinary businesses and callings are open to those who wish to enter them; the state can only prescribe reasonable conditions upon which permits are to be had.⁴⁵ If the ginning of cotton were an ordinary business, Frost's license would grant him no other right than to compete with other gin-

berland Telephone Co., 230 U. S. 58, 33 Sup. Ct. 988 (1913); *Boise Water Co. v. Boise*, 230 U. S. 84, 33 Sup. Ct. 997 (1913); *McPhee & McGinnity Co. v. Union Pacific R. R.*, 158 Fed. 5 (C. C. A. 8th, 1907).

⁴³ In this case a great deal of attention is given to legislative classification; it invites study as an example of judicial classification. It is interesting to note the things which the legislature distinguishes; it is of equal interest to observe the things which the court associates. It may be remembered that in a recent case the concept "brokerage" was used by the court to get the dealer in theatre tickets and the employment agent in the same class. *Ribnik v. McBride*, 277 U. S. 350, 48 Sup. Ct. 545; see Comment (1928) 38 YALE L. J. 225. Here a like concept, not given a specific name, is used to get cotton gins in the class of railroads and water works. Some extreme critic is certain to insist that the logical principle underlying Mr. Justice Sutherland's reasoning is that what is true of all the members of a class is true of a member of a different class.

⁴⁴ For judicial utterance upon the right of the state to grant, to modify, and to terminate a franchise right see: *Louisville Bridge Co. v. United States*, 242 U. S. 409, 37 Sup. Ct. 158 (1917); *New Orleans Gas Co. v. Louisiana Light Co.*, 115 U. S. 650, 6 Sup. Ct. 252 (1885); *New Orleans Waterworks Co. v. Rivers*, 115 U. S. 674, 6 Sup. Ct. 273 (1885); *Shallenberger v. First State Bank*, 219 U. S. 114, 31 Sup. Ct. 189 (1911); *Dillingham v. McLaughlin*, 264 U. S. 370, 44 Sup. Ct. 362 (1924); *Denver v. New York Trust Co.*, 229 U. S. 123, 33 Sup. Ct. 657 (1913). For a discussion of the legal character of "the certificate of convenience and necessity" see *Lilienthal & Rosenbaum, Motor Carrier Regulation by Certificates of Necessity and Convenience* (1926) 36 YALE L. J. 163, 166-171.

⁴⁵ *Yick Wo v. Hopkins*, 118 U. S. 356 (1886); *Quong Wing v. Kirkendall*, 223 U. S. 59, 32 Sup. Ct. 192 (1912); *Adair v. United States*, 208 U. S. 161, 28 Sup. Ct. 277 (1908); *Truax v. Raich*, 239 U. S. 33, 36 Sup. Ct. 7 (1915).

ners for trade, and the application of the Durant Cooperative Company for a permit could not be refused. In that event the argument about a denial of "the equal protection of the laws" could not be validly raised. If Frost's rights are something more, or if a license is not easily to be had by the Durant Cooperative, it must be because the ginning of cotton is a public business. But there is in its nature nothing to distinguish it from the milling of grain, the supply of credit, or the sale of fertilizers, upon all of which the farmers of Oklahoma are dependent, and all of which are open and competitive businesses. If legally it has been put in a distinct class it has been by act of the state legislature;⁴⁶ that the legislature has the power to divest the business of its public character does not seem to be denied.⁴⁷ In last analysis the right of Frost, however broadly it may be interpreted, has its source in a legislative declaration which is admittedly subject to modification or repeal; the right of the Durant Company to a permit rests upon the act of the same law-

⁴⁶ To one familiar with the decisions of the present Court, the assumption in the present case that because of legislative declaration the ginning of cotton is a "public business" is a bit perplexing. If a "public business" is a distinct legal category, it would seem to lie between a business "affected with a public interest" and a "public utility." The ginning of cotton, a competitive industry, fails to meet even the criteria laid down for a business "affected with a public interest." "The business must be such 'as to justify the conclusion that it has been devoted to a public use and its use thereby, in effect, granted to the public.'" Mr. Justice Sutherland, in *Ribnik v. McBride*, *supra* note 43, at 355, 48 Sup. Ct. at 545. Moreover, "the mere declaration by the legislature that a particular kind of property or business is affected with a public interest is not conclusive upon the question of the validity of the regulation." Mr. Justice Sutherland, in *Tyson & Bro. v. Banton*, 273 U. S. 418, 431, 47 Sup. Ct. 426, 428.

⁴⁷ It will perhaps help to clarify the matter to ask what the decision of the Court would have been had the validity of the legislative declaration that the ginning of cotton is a public business been raised. There were technical difficulties in the way of raising the issue in the instant case, into which it is here not profitable to go. But it might have been raised in a suit in which a person engaged in cotton ginning went into court for protection against the authoritative regulation of his charges under the act of 1915. It is difficult to see, in view of the decision in the *Ribnik* case, how the statute could be upheld; for if employment agencies are not "affected with a public interest," surely cotton ginning is not a "public business" for purposes of price control. It might possibly be held to be such on the authority of *Munn v. Illinois*, 94 U. S. 113 (1876), and *Cotting v. Kansas City Stock Yard Co.*, 183 U. S. 79, 22 Sup. Ct. 30 (1901), for it is easy to associate cotton gins with grain elevators and stock yards either by physical analogy or by a likeness in function. Such an association, needless to say, would not be based upon considerations relevant to the need for regulation and the appropriateness of its form, and it would do violence to outstanding differences between the industries. Grain elevators and stock yards which stand at "the great gateways of commerce" raise one problem of control, and cotton gins which plentifully dot the landscape quite another.

making body. The constitutional issue of "the equal protection of the laws" is evoked only by using the "public business" statute to invalidate the proviso which makes mandatory the granting of a permit to a cooperative association upon the petition of the "one hundred citizens and taxpayers."⁴⁸ It is difficult to see why of two rights, emanating from separate acts of the same legislature, one is valid and the other invalid. Many careful students of the case are likely to conclude with Mr. Justice Brandeis that the result is reached by a conversion of the right to gin into "a limited immunity from the competition" of other ginners.⁴⁹ There is certain to be a respectable agreement with Mr. Justice Stone that inasmuch as Frost already had a license which was not an exclusive permit, he had no "constitutional ground" on which to "complain of a discrimination from which he has not suffered."⁵⁰

But of far greater importance is Mr. Justice Sutherland's defensive argument. To those concerned with the cooperative movement the principal question is ahead; these issues which make up the main argument are mere preliminaries. The minority of the Court insists that even if permits to gin are issued to individuals and to cooperatives upon different terms, there is no denial of "equal protection of the laws," for such a distinction is "proper classification" and well within legislative discretion. It is in attack and defense at this point that the nature of the cooperative association, its social function, and the form of its organization receives judicial attention.

The spokesman for the Court admits that a distinction resting "upon some ground of difference having a fair and substantial relation to the object of the legislation" is valid. But he insists that the distinction in question is "without any such basis" and "arbitrarily favors the corporation," *i.e.*, the cooperative association, "as against the individual." He has "no reason to doubt" that a distinction between a private business and "an association for mutual help, without capital stock, not conducted for profit, and restricted to the business of its own members . . . might properly be upheld." It chanced, however, that the Durant Company "has capital stock . . . is allowed to do business for others; to make profits and to declare dividends." In fact it is "in no sense a mutual association. Like its individual competitor it does business with the general public for the sole purpose of making money." So it is that "the proviso as here construed and applied boldly creates one rule for a natural per-

⁴⁸ It is, of course, easy to interpret the legislation in such a way as to make the petition of "one hundred citizens and taxpayers" the "showing" of public necessity.

⁴⁹ *Frost v. Corporation Commission*, *supra* note 1, at 241.

⁵⁰ *Ibid.* 248.

son and a different and contrary rule for an artificial person." In short, without violence to the equal protection clause, a line cannot be drawn between business ventures and cooperative associations. The line must be drawn, if drawn at all, between individuals, corporations, and cooperative associations organized as corporations on one side and mutual benefit societies on the other.⁵¹

The immediate impression made by this argument is the uncertainty of its terms. It makes it quite impossible to determine what legislative distinctions may and what may not "be properly upheld." It seems to be based upon the assumption that all cooperatives fall into the two clear-cut and mutually exclusive groups of business corporations and mutual benefit societies. The criteria actually used are three in number, the use or non-use of capital stock, the conduct of the venture for profit or not for profit, and the doing of business or not doing of business for non-members. But an association may possess capital stock and not be run for profit, it may not possess capital stock and be run for profit; it may be run for profit and not serve non-members, it may not be run for profit and serve non-members; in fact these different elements may be put together in various permutations. Nor are the meanings of the several terms clear beyond peradventure. A share of stock may confer upon its holder only a contingent right to a dividend; it may entitle him to a vote in the election of directors and carry no claim to a pecuniary income; it may combine a claim upon profits with a share of control in many different ways. An association may be organized to serve the pecuniary interests of its members and yet neither aim at profit nor pay out dividends. Profit and dividends are technical terms and the forms that pecuniary gain may take are many and various. A cooperative society may not do business for non-members and yet have subsidiaries that do; there are many ways by which it can advance its interests by making use of outsiders without engaging in traffic with them directly. Most important of all, capital stock, profits, doing business for outsiders, what not, are mechanical devices and procedures. They belong to the domain of form and structure; they tell little of the ends, the nature, the manner of doing business, or the worth of the enterprise in which they are employed.

But, whatever the criteria employed, the clear-cut distinction of the opinion finds little support in the realities of cooperative organization. It is quite impossible to find a pure example of a mutual benefit society. It is a matter of common knowledge that farmers do not band themselves together for purposes of brotherly love alone; their end is to advance their material and pecuniary interests. It is only when the association loses its own

⁵¹ *Ibid.* 233-239.

distinctive features that it becomes a business corporation. A careful study of cooperatives reveals a great variety in structure; in nearly all of them are to be found elements alike of voluntary cooperation and of business enterprise. Nor could it well have been otherwise. The end has been association for self-help; but the activities in which they engage are business activities; if they are to survive it must be in a world in which industries are under business control. Since their problems of financing, of marketing, of winning and holding patronage are much like those which every business must face it is almost inevitable that they should borrow the devices and procedures of business. The use of the corporate form simplifies the problem of organization and avoids many a complicating legal tangle. The issue of stock is a simple and obvious procedure for securing a necessary capital.⁵² The device of profits is a way of distributing the gains from the economies in marketing which it is the object of the association to effect. The service to non-members is a part of a policy for leading lukewarm individuals into the fold. But such elements of business as these are mere devices; their employment does not mean the exclusion of alternative arrangements; they may all be employed by a cooperative without any sacrifice of its purposes or character and without turning it into an ordinary business corporation.

In fact it is just this borrowing of the devices of business and the adaptation of them to the end of cooperation which has been going on. Neither capital stock, nor profits, nor service to outsiders is incompatible with the establishment among constituent members of "economic democracy on lines of liberty, equality and fraternity." Where capital stock is used, the voting privileges are not those of the business corporation; there is in use "the cooperative principle" of "one man, one vote." In the election of directors the amount of the member's holdings avails him nothing. There are likewise restrictions on the transfer of stock certificates. In many cases shares held by non-patronizing members carry fixed rates of return, confer no voting privileges, and partake in reality of the character of bonds. Where the device of profits is used, the rate of return is generally limited, in most

⁵² Such cooperatives as creameries, cheese industries, and grain elevator companies, etc. require more capital and in more concentrated, immediate amounts.

As the proof is being read there comes to hand MONTGOMERY, *THE CO-OPERATIVE PATTERN IN COTTON* (1929), a book which presents in clearcut perspective and with fullness of detail the general situation out of which the Frost case emerges. It contains a graphic account of the attempt to contrive a form of organization which will at once meet the farmers' need for mutual help and insure easy going in the world of business in which products have to be sold. It is unfortunate that the book came from the press too late to be used in the preparation of this article.

cases to eight per cent; the disbursements to members is graduated in terms of the amount of custom secured from each; and excess profits are apportioned to "an increase in capital," appropriated to "educational or provident purposes," or distributed as "patronage dividends." Almost without exception, whether using or not using the devices of capital stock and of profits, cooperative associations do business for outsiders.⁵³ The Oklahoma law, under which the Durant Cooperative was organized, imposes such limitations as these upon the use of business devices by cooperatives. Thus the associations organized under state laws tend towards a common type, which is quite unlike the commercial corporation. In a word "a new and different unit" for the doing of business has been in process of development.

In the development of this distinctive form of association the legislature and the judiciary have had their parts. In thirty-three states acts provide for the limited use by associations of the devices of the business corporation.⁵⁴ It is of note that whereas exemption from prosecution was under the Clayton Act limited to associations organized for mutual benefit and without capital stock,⁵⁵ by the Capper-Volstead act the immunity was extended to the new type of organization.⁵⁶ The power of the state to promote the interests of farmers by appropriate legislation and to resort to classification for their especial benefit has been repeatedly recognized by the courts.⁵⁷ In the *Liberty Warehouse* case⁵⁸ the United States Supreme Court dismissed the contention that the Bingham enabling act⁵⁹ was invalid under the Fourteenth Amendment with the words, "it is impossible to say that the legislature of Kentucky could not treat marketing contracts between the association and its members as of a separate class." The Burley Cooperative Association, a party to that suit, had no outstanding capital stock, but its subsidiaries engaged in warehousing were organized as corporations. In the opinion of the Court not a single case is cited in which a previous distinction

⁵³ With this account compare Mr. Justice Brandeis' dissenting opinion, *Frost v. Corporation Commission*, *supra* note 1, at 243-247.

⁵⁴ See Mr. Justice Brandeis' opinion, *ibid.* 244, n. 12.

⁵⁵ 38 STAT. 731, § 6 (1914) 15 U. S. C. § 17 (1926).

⁵⁶ 42 STAT. 388 (1922), 7 U. S. C. c. 12 (1926).

⁵⁷ But Mr. Nourse had issued a warning that seems well-taken in the light of the instant case: "A scrutiny of the various judicial opinions shows clearly that the framing of co-operative statutes so as to apply to a single class does raise an issue which, although it has been successfully fought out before many state courts, has presented to opponents of the co-operative system a promising line of attack." NOURSE, *op. cit. supra* note 12, at 413.

⁵⁸ *Liberty Warehouse Co. v. Burley Tobacco Growers' Cooperative Marketing Ass'n*, *supra* note 19.

⁵⁹ See *supra* note 15.

had been made between cooperatives upon the basis of the use or non-use of some device or procedure of a business corporation. The most striking thing about Mr. Justice Sutherland's opinion is that the cooperative association is not recognized as a distinct business unit; it is lost in an over-simple and unreal separation of "corporations" from mutual benefit societies.

It is evident that the decision in the *Frost* case is of great significance; but, because of the uncertainty of the holding, it is indeed hazardous to attempt to reduce that significance to specific terms. An isolated rule, unbuttressed by precedents, and connected with the general body of law only by an attenuated train of argument, is always a disturbing thing. It is, perhaps, no fault of Mr. Justice Sutherland that he has not been able to fortify his conclusion by a less perplexing course of reasoning. The great jurists who have done creative work have frequently moved faster than they could bring up their reasons. The positions taken by Mr. Chief Justice Marshall are today regarded as generally sound; but his arguments are to many persons far from compelling. The future proved Mr. Chief Justice Taney sound in the *Charles River Bridge* case,⁶⁰ but at the time he had only a vague appreciation of the doctrine of the police power which he used to reach his result. In declaring the Granger legislation valid,⁶¹ Mr. Chief Justice Waite gave a forward-looking judgment; but his argument is not well put together and his handling of the concept of "public interest" by no means deft; the wrong-headed opinion of Mr. Justice Field is a far neater exhibition of dialectic. Like his distinguished predecessors, Mr. Justice Sutherland's great virtue is in an ability to take a radical position; his fault is the fault of the innovator, who can do no more than his best in connecting a far-flung outpost with the established domain of the law. It is to be expected that Mr. Justice Brandeis and Mr. Justice Stone, with their unwillingness to depart too far from the course marked out by precedent, their sensitiveness to existing fact, and their respect for competition as an established social policy, would be able to muster the more sufficient reasons. But the merits of their opinions are those of sturdy conservative arguments. If the decision is perplexing and provoking it is because of the great hinterland which lies between former judicial utterance and the decision in this case. Until this is reduced to law and order the exact meaning of the judgment in the *Frost* case cannot be known.

For that reason those who guide the cooperatives can in no certain way accommodate their policies to the most recent decision. So far as the holding and even the dicta go, though they cannot

⁶⁰ *Charles River Bridge v. Warren Bridge*, 11 Pet. 420 (U. S. 1837).

⁶¹ *Munn v. Illinois*, *supra* note 47.

certainly be distinguished, the situation can be met. Capital can be raised in other ways than by an issue of stock; gains can be disbursed, even if "profits" and "dividends" be under the ban; some device, such as associate membership, can be contrived to enable outsiders to be insiders for the purpose of doing business with the association. A cooperative corporation may be converted into a non-stock, not-profit-making society without a sacrifice of current ends, methods, or procedures. The net effect of it all will be to force the association to use crude devices instead of effective ones, to employ circumlocution in place of straightforward action. Nor does the decision impose a serious barrier against those who would attack Frost's monopoly; the protection accorded his property right, which has its basis in a structural distinction between kinds of cooperatives, rests upon no secure foundation. Nor, so far as it affects entrance into an industry, does the decision of necessity force the cooperative association to put off the form of a business corporation. The state legislature, by divesting the ginning of cotton of its public character, may permit farmers' associations to win for themselves whatever trade they can get in competition with any and all comers.⁶² But the abruptness with which this decision comes, its isolation from the general body of law, and its failure to recognize the cooperative association as a distinct form of organization indicate that there are judicial hazards ahead which are all the greater because they cannot be clearly foreseen.

A judgment upon the measure of wisdom which the decision holds must be left to the course of events. But it is at least interesting to note in its wake some very curious things. A state attempts to reduce an unruly industry to order and succeeds in endowing with privileges individuals it sought to control. It is balked in an attempt to give cooperatives an opportunity to bring ginning under responsible direction by affecting the business with a public character. To sanction an experiment designed to secure for an important industry the most suitable form of organization, it must divest the business of its public character. A legislative declaration that the ginning of cotton is a public business converts a right to compete into a limited

⁶² It is hard to see how an act of the legislature divesting the ginning of cotton of its character of a public business could be directly challenged. Nor would the owner of a license granted under the statute repealed have an opportunity to bring suit to prevent the cancellation of his license; for the act of divestment would leave him secure in his right to compete. It is, of course, possible that claiming it to be a franchise, he might seek protection for his "property right" by asking the court in effect to declare the divesting act invalid. But, the instant case aside, no precedent in point has been discovered, and such an outcome seems unlikely. If it came to pass, the perpetuation of a host of such franchises would constitute an ironical memorial to an attempt at regulation which had failed.

immunity from competition. An individual has his conditional privilege to monopoly sanctioned by an invocation of "the equal protection of the laws." Some critic, unblessed with prophetic foresight, is sure to discover in the case only the creation of property by a very mysterious process of law.