Shipping Conference Dual-Rate Contract Arrangements as a Competitive Weapon

Jon Magnusson
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LITIGATION pitting the predecessor agencies of the Federal Maritime Commission against the Department of Justice has been, for many years, the deplorable fare for lawyers engaged in the regulation of the ocean shipping industry. The intellectual raw material of the disputant federal agencies may provide grist for the slow, fine-grinding mills of bureaucracy with a by-product of rich, controversy-centered news, but the end products of this milling operation have only been expense, delay and uncertainty for the regulated shipping lines.

The attack in the courts has been aimed at achieving pre-eminence of a congressional anti-trust policy over an explicit congressional policy of accommodating our shipping lines' business practices to those of the rest of the world. Perhaps these two congressional policies are at war with

† B.S. University of Virginia; LL.B. George Washington University Law School; Member of New York, Virginia and District of Columbia Bars; Special Assistant to Commissioner John S. Patterson of the Federal Maritime Commission.

The views expressed are those of the author and not necessarily those of the Federal Maritime Commission.

There is absolutely no present antagonism between the Department of Justice and the Federal Maritime Commission. This article deals solely with past issues. In the past, opposing positions have been taken on the issues discussed herein. Whether or not such positions would be taken on any future issues is impossible to say.
themselves. If so, some conflict is inevitable. In any event, no prominent effort has been made to end this wasteful disputation. Whether inevitable or unresolvable, the purpose here will be to suggest a line of effort toward a little peace and harmony between two distinguished agencies.

The chief obstacle to even a beginning at any solution are factors beyond congressional control in the form of a stubborn refusal by nationals, outside our jurisdiction, to accept what they regard as our self-righteous notions of business morality. Yet, implicit in at least one of the ambivalent congressional policies is a realistic recognition that internationally we are outweighed in influence, if not in high-mindedness. The subject of the fight is the validity of entrenched and venerable trade practices which evolved out of business necessities when steam-powered, self-propelled ships replaced sailing ships in ocean commerce among nations. One side seeks to impose our policy of opposing price-fixing agreements and combinations in restraint of trade on the activities of rate-fixing associations or conferences of steamship lines. The other side seeks to preserve these organizations and their exclusive patronage contracts as a useful device for the conduct of world shipping in areas where our virtuous policies do not prevail.

Two lines of attack have emerged to impose the antitrust morality on these trade practices. One line is to promote court-sanctioned interpretations of law to forbid conferences of ocean carrier shipping lines from fixing freight rates. If this fails, the next line is to invalidate or control conferences' practices of using exclusive patronage contracts with shippers as a condition of getting discounted freight rates. The attack on the contract is the subject of this article.

The suggestion is offered that if more is known about the genesis and purpose of traditional international trading practices a resolution of the conflict may be possible. If not, at least excessive zealotry in regard to proper national policy may be restrained at a saving of litigious energy and money, and harmony and contentment promoted.

There seem to be at least three lines of thought about how to deal with exclusive patronage contracts. One of
the doctrines is that when a number of steamship lines, associated together in a conference, adopt two levels of freight rates and offer lower or discount rates to shippers who sign an exclusive patronage contract with the conference and the higher to non-signers, the conference is necessarily acting unlawfully by engaging in an oppressive competitive practice, or by stifling competition or by using a retaliatory device.\(^1\) The expression used is that this trade practice, commonly called the dual-rate system, is unlawful per se.\(^2\)

Another line of thinking is that the trade practice is a legitimate accommodation to the needs of shippers, and a method of self-preservation for the conferences which is sanctioned by the Shipping Act of 1916, \(^3\) hereafter referred to as the Act.

A third line of thought recently proposed is that the coercive effect of the practice be recognized, and that its use be authorized to meet and oppose the coercive effect of non-conference cut-rate competition.\(^4\) In this view the practice is not necessarily illegal if it is shown to be a necessary retaliatory competitive measure. This emphasis on the necessities of each position typifies the paucity of facts and soundly-based arguments on the subject.

The conflicting arguments and the resulting uncertainties from these divergent interpretations pose a serious problem for ship lines faced with a necessity of making arrangements with shippers under assurances that they are acting in conformity with the law and particularly with the new

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\(^1\) The doctrine has been expressed as follows: "Use of a dual-rate system by a conference is essentially coercive and discriminatory as to shippers and exclusionary as to carriers." Statement by Mr. Kirkpatrick, Acting Attorney General, before Celler Committee quoted in Hearings Before the Special Subcommittee on Steamship Conferences of the House Committee on Merchant Marine and Fisheries, 87th Cong., 1st Sess. 57 (1961).

\(^2\) Brief for Petitioner, p. 2, Federal Maritime Bd. v. Isbrandtsen Co., 356 U.S. 481 (1958), framed the basic question as being: "Whether the dual-rate system of ocean freight rates . . . is per se illegal under the Shipping Act of 1916 and therefore beyond the power of the Federal Maritime Board to approve under Section 15 of that Act."


congressional enactments. Some of the supporting arguments and the circumstances out of which the conflicts arose and recent legislative changes will be reviewed. It will be shown that even though traditionally acceptable business practices and implementing contracts, as approved by the courts, validate most exclusive patronage contract schemes using two levels of freight rates, more evidence should be obtained as to the extent of the shipping business practices around 1916 to find out whether or not Congress intended to condemn the practices to the same extent that it intended to condemn the use of rebates, fighting ships, retaliation, discrimination and other unfair methods which are more specifically mentioned in the Act. It will be proposed further that if the necessary competitive measure justification for retaliation or coercion is adopted, and if recent court decisions are extended, the results may be disastrous for shipping conferences.

Inferences and assumptions about the dominant purposes of the attacked practices are now used to support arguments for each position. The purpose of obtaining the new evidence would be to substitute facts for what is now inferred or assumed, and to test the validity of some of the positions proposed herein. Such fact gathering would be the task of a congressional committee as legislation may eventually be needed to clarify the problem if current arguments are pushed to their conclusion.

The new strength of arguments against the validity of present practices is of recent origin. Until 1956, legitimacy had been the dominant view judging by the absence of any express statutory prohibition or judicial decision of illegality and the continued use of the practice. Generally, the

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5 75 Stat. 764, 46 U.S.C. § 812 (Supp. III, 1961) provides that “existing agreements which are lawful . . . immediately prior to enactment of this Act, [before October 3, 1961] shall remain lawful . . . Provided, however, That all such existing agreements which are rendered unlawful, by the provisions of such Act as hereby amended must be amended . . . and if such amendments are filed for approval within six months after the enactment of this Act, [April 3, 1962] such agreements so amended shall be lawful for a further period of not to exceed one year [April 3, 1963] after such filing.” Pub. L. No. 88-5 deleted the words “of not to exceed one year after such filing” and substituted “but not beyond April 3, 1964.” 77 Stat. 5 (1963).
practice has been considered to be sufficiently consistent with statutory provisions to warrant approval by the Federal Maritime Commission, and its predecessor agencies. More recent history, however, has shaken some of the assumptions underlying these trade practices and of their approvable under Section 14b in the recent amendments of the Act.  

In 1956 the proponents of the line of thought condemning all such agreements as coercive seemed to have finally scored a victory. In *Isbrandtsen Co. v. United States*, the Court of Appeals for the District of Columbia held that the use of a dual-rate contract was prima facie discriminatory. The circumstances were that associated member lines of the Japan-Atlantic and Gulf Freight Conference had been competing along the same trade routes with the Isbrandtsen Company, a steamship line which was not a member of the conference and which refused to become a member. The court, in striking down the use of a dual-rate system, stated that since the provisions of the shippers' contracts "are unlawful the system containing them cannot validly be approved by the Board." It was also noted by the court that the dual-rate system constituted retaliation, and as such must be condemned without regard to the question of reasonableness.

The Supreme Court affirmed this decision by agreeing that the order of the Board approving the contract system of the Japan-Atlantic and Gulf Freight Conference should be set aside. The language of the Court's decision left considerable doubt. It is not certain whether it adopted and endorsed the circuit court's general condemnation of the conference practice as unlawful or just decided that since the Board had found that the dual-rate contract of the conference was a necessary competitive measure to

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8Id. at 937.
9Id. at 938.
offset the effect of non-conference competition in order to obtain for its members a greater participation in the cargo moving in the trade; it follows that the contract was a resort to other discriminating or unfair methods to stifle outside competition in violation of Section 14 Third of the Act.\textsuperscript{11} The doubts were created by the dissenting opinion which stated that “the Court thus outlaws a practice that has prevailed among international steamship conferences for half a century” when the majority held that “any dual system of international steamship rates tied to exclusive patronage contracts that is designed to meet outside competition . . . violates § 14 of the Shipping Act. . . .”\textsuperscript{12} On the other hand, there are those who think the majority’s qualification as to practices “designed to meet outside competition” is significant. In recognition of the qualification, Congress enacted legislation to forestall any completely invalidating effect of the Court’s decision on the trade practice, as implied by the dissent.

The most recent development affecting the trade practice is the addition of Section 14b to the Act which, for the first time, expressly refers to contracts that provide lower rates to shippers who agree to give their patronage to a carrier or conference of carriers and authorizes the Federal Maritime Commission to give permission for their use. The new law did not provide any standards for judging detriments to commerce or contrariety with public interest. Therefore, in light of the dissenting opinion that the practice has been outlawed, those who would argue that no standards are needed because the practice is necessarily unlawful under Section 14 Third and argue that the burden is on the proponents to show standards of lawfulness seem to have the offensive.\textsuperscript{13}

\textsuperscript{11} Id. at 492.
\textsuperscript{12} Id. at 500 (dissenting opinion). The outlawry characterization by the dissenting justice is shared by at least one writer on the subject when he concluded: “the Supreme Court . . . held that the contract rate system was a retaliatory device forbidden by section 14.” Gardner, \textit{Steamship Conferences and the Shipping Act, 1916}, 35 Tul. L. Rev. 129, 133 (1960).
\textsuperscript{13} The position of the Department of Justice concerning the new legislation has been stated as follows: “The Department of Justice considers indispensable . . . the inclusion of language unequivocally barring the approval
This article will examine the validity of the newly strengthened "necessary unlawfulness" argument by reviewing in detail recent history showing what the practice consists of in its present form, the events which caused the practice to be condemned by the Supreme Court, the events following the Isbrandtsen decision leading to the amendment of the Act and the law as it now stands. This review of recent history will be compared with the earlier history of the practice in an effort to see if anything turns up which might be useful in establishing standards for future action under Section 14b of the Act.

In its present form the practice consists of a two level, or discount, tariff system plus an agreement among conference members to prepare and tender a standard form of shippers' contract with the conference. Pursuant to the contract, the conference members collectively agree to take and carry all the shippers' merchandise at the specified freight rates and the shippers agree not to patronize, for a specific period, any other than the conference lines. This is the plan that is thought to be illegal unless some beneficial competitive purpose is shown.

Normally, an agreement among shipping conference lines to fix rates would be void as against the public policy of this country. The conference lines agree among themselves on the rates to be charged shippers, on the terms of exclusive patronage contracts, and on the differentials to be offered shippers who sign contracts and those who do not. They agree to restrain competition among each other for shippers' cargoes and otherwise to control, through their monopoly over part of the trade, the conditions relating to the carriage of shippers' property. The conference contracts become consistent with our public policy if the conferences file their agreements of association and statements about their "contract—non-contract rates" plans with the Commission and obtain its approval. The contracts are thereafter excepted from the anti-trust laws which make

of such agreements where they are intended to or will reasonably likely cause the exclusion of another carrier from the trade." Letter from Byron White, Deputy Attorney General, to Senator Magnuson, Aug. 8, 1961.
them otherwise illegal.\textsuperscript{14} Section 15 of the Act creates this exception on the condition of approval.\textsuperscript{15} Before the Commission may give its approval it must decide that the agreement of association does not violate the Act, and is not "unjustly discriminatory or unfair as between carriers, shippers, exporters, importers, or ports, or . . . operate to the detriment of the commerce of the United States . . . ." \textsuperscript{16}

Against this background, one of the most controversial and significant litigations in the history of the administration of the Shipping Act began after the former Board approved a conference statement proposing to institute its contract-non-contract rates plan. In December 1952 such an approval was applied for by the Japan-Atlantic and Gulf Freight Conference. This was the first critical move bringing official focus on the events culminating in the Supreme Court's condemnation of the conference's plan in the \textit{Isbrandtsen} case. The application for approval was pursuant to the Board's General Order No. 76. Protests against the application were filed by Isbrandtsen and by the Department of Justice. Institution of the practice was enjoined in the courts. A little over three years later the Board, after being taken to the courts on procedural issues,\textsuperscript{17} ordered "that the agreement embodied in and constituting the aforesaid statement filed by the . . . Conference . . . be, and the same is hereby, in all respects approved under Section 15 of the Shipping Act . . . ."\textsuperscript{18} In support of its order, the Board found that from 1928 through 1941 "the conference employed a dual-rate system,"\textsuperscript{19} and that in 1934 the system was extended "to cover all important commodities moving in the trade."\textsuperscript{20}

\begin{footnotes}
\item[19] Id. at 710.
\item[20] Ibid.
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In 1947, Isbrandtsen began operating from Japan to Atlantic coast ports, but refused to join the conference. At this time the so-called dual-rate system had not been re-activated. Isbrandtsen's competition in the form of lower rates during this period was found to be the subject of constant concern for conference members, and, in March 1953, rates were "opened" which meant that each conference member line made its own rates instead of using conference rates. Individual lines could now undercut Isbrandtsen's rates. The Board noted that after July 1953, Isbrandtsen carried little cargo in the trade.

Before 1953 there occurred a phenomenon that has never really been explained satisfactorily—concern over competition during a period of increasing rates. In spite of the findings of competitive necessity for what had happened during the period from 1947 on, the Board stated that "the level of rates in conference post-war Tariffs gradually increased between 1947 and November 15, 1952." Afterwards, in March 1953, genuine rate reductions, directed at independent competition, occurred resulting in the disappearance of business for Isbrandtsen in July 1953. Rate reductions between March and July 1953, and not competitive conditions in the preceding five years, apparently drove Isbrandtsen out of the trade. The conference asked for approval of its plan to offer the exclusive patronage contract with two rate levels in December 1952, but the disappearance of Isbrandtsen's business cannot be traced to this move because the conference did not receive approval until January 1956. Operation of the practice before that time had been enjoined.

The Board's rationalization of its approval required a choice between only two justifications—competitive necessity or excessive rate reductions—but seldom has such a simple choice had such drastic and far-reaching consequences. The long period of conference concern with Isbrandtsen competition led the Board in its report to ask itself: "Is the initiation of a dual-rate system necessary or required, as

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21 Id. at 713.
a competitive measure, to insure or restore stability of rates and service to shippers in the trade . . . ?” The Board answered its own question, finding that the inauguration of a dual-rate system was a necessary competitive measure to offset the effect of independent competition in this trade. The Board’s order followed up this conclusion by approving the conference’s application “to institute a dual-rate system in this trade . . . effective January 1, 1956.” The Board’s choice of the “necessary competitive measure” justification turned out to be crucial. On the facts before it, as disclosed in its own report, the Board might well have found rate cutting and chosen to regard this fact as the damaging competitive measure, not the exclusive patronage contracts and dual-rate system. The Board might have approved the contract dual-rate system, which was in effect in some form since 1928, simply as a legitimate trade practice having no essential relation to competition in this case. The die was cast, however, and the Board’s choice provoked long and expensive litigation for the respondent conference and uncertainty for the entire shipping industry for years to come, because it reached right into the nerve center of an historic and well-entrenched trading system.

Isbrandtsen’s response, joined by the Department of Justice and the Department of Agriculture, was to appeal the decision in the courts, with the claim that the Board had no authority to approve a dual-rate system because it would be in violation of the Act as a discriminatory and retaliatory measure. The Supreme Court ended court consideration of these controversial issues when it reversed the Board’s order in a decision which immediately provoked discussion of its true scope and intent.

The scene of subsequent events shifted from the courts to Congress. Congressional reaction to the Isbrandtsen decision was prompt, but as it turned out, no more clear than the decision. Hearings on the effect of the decision were started by the Senate Committee on Interstate and Foreign Commerce. The Committee proposed legislation to

22 Id. at 736.
overcome some of the effects of the decision. After taking note of the lack of clarity in some of the Court's language, the Committee predicted widespread confusion and endless litigation. To eliminate any bad effects of widespread confusion and to curb litigious impulses to determine the decision's full impact on traditional practices, the Committee proposed, and Congress enacted, legislation declaring valid "any dual-rate contract arrangement in use . . . unless [the Federal Maritime Board] disapproves, cancels or modifies such arrangement." The validation applied to "any dual rate contract arrangement in use by members of a conference on May 19, 1958, which conference is organized under an agreement approved under Section 15 of this Act. . . ." The legislation, approved August 12, 1958, was construed to limit invalidity to the actions of the Japan-Atlantic Conference and to validate the arrangements of other conferences, whose contracts had been theretofore approved by the Board. The congressional limitation was to last only until the Board had gone back and reviewed all previously approved arrangements and reached new conclusions about whether they involved necessary competitive measures to offset the effect of non-conference competition.

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25 In the Matter of Pasch, 26 Misc. 2d 918, 209 N.Y.S.2d 191 (Sup. Ct. 1960), aff'd mem., 13 App. Div. 2d 470, 214 N.Y.S.2d 283 (1st Dep't), motion for leave to appeal granted, 9 N.Y.2d 965, 176 N.E.2d 502, 218 N.Y.S.2d 47 (1961). The court stated: "The legislative history of this amendment makes plain the intention of Congress, by this legislation, to provide the industry with a moratorium during which Congress might study and investigate, to the end that appropriate legislation might thereafter be enacted. Petitioner asserts the amendment preserves the validity of the dual-rate contracts now under consideration. Respondents argue to the contrary and contend the amendment was intended to do no more than preserve the status quo that had been disturbed by the adjudication of the Supreme Court of the United States in the later Isbrandtsen case; that it was not the intention of Congress to limit the effects of the adjudication in the earlier Isbrandtsen case, and, as a consequence, the amendment must be deemed to include the qualification that exclusive patronage dual-rate contracts must, in any event, have been approved by the Federal Maritime Board to acquire validity. I reach a different conclusion. Respondents' contention as to the meaning of the amendment works a distortion in the language employed by Congress which plainly states . . . unless and until such regulatory body disapproves, cancels or modifies such arrangement in accord—
idating legislation by its terms expired June 30, 1960, thus providing, according to the Committee's report, "what is considered to be a reasonable time for a thorough consideration of the procedures necessary to resolve the dislocation resulting from a recent Supreme Court decision." This hope proved to be overly sanguine and another extension had to be granted because the House Committee on Merchant Marine and Fisheries, which was also considering remedial legislation, found it "impossible to digest the voluminous records in order to prepare a report" or to recommend legislative action after eighteen months of "holding hearings and making an intensive study into the problems which have been presented." More legislation extending the validation of the dual-rate practices until June 30, 1961, was enacted. When the expiration date arrived the digestion problem continued to be as difficult as ever, and, as a remedy another extension until September 15, 1961, was prescribed. Still another dose of deferral until October 15, 1961, had to be taken. Each prescription for the relief of congressional digestive difficulties came as a narrow escape from the uncertain and litigation-inducing effects of the Isbrandtsen decision. The first extension was approved by the President and became law June 29, 1960, the day before expiration; the second, on June 30, 1961, the day of expiration; the third, on September 16, 1961, the day after expiration; and the fourth brought final legislative relief on October 3, 1961, a record-making twelve days before the last extension expired.

ance with the standards set forth in section 15 of this Act.' It would have been a simple matter for Congress, if it desired to do so, to insert appropriate language in the amendment limiting the validity of the dual-rate contracts to those actually approved by the Board. It is incredible to assume that Congress was wholly unaware of the earlier Isbrandtsen case when it enacted the legislation. I conclude Congress neither intended nor desired to limit the effect of the amendment in the manner suggested by respondents.”

Id. at 924, 209 N.Y.S.2d at 197.

26 S. REP. No. 1497, 86th Cong., 2d Sess. 16 (1960).
The desperation caused by congressional inability to find a cure for its digestive distress was vividly shown in the last extension to October 15, 1961, which, with a mighty reach for maritime relevance, was made a part of a law to make the Panama Canal Company immune from attachment or garnishment of salaries owed to its employees and "to amend the Shipping Act, 1916." 32 Any digestive distress of congressional committees during this period, from August 12, 1958, to October 3, 1961, can hardly match the ulcer-inducing conditions that must have been faced by many industry leaders confronted with doubts as to the validity of long-standing trade practices and with expensive litigation in this period. The leaders should also have been concerned with the results of the Federal Maritime Board's review of their dual-rate contract arrangements for conformity with the Isbrandtsen decision's interpretation of the Act in response to the congressional reprieve. A few invalidating orders might be expected.

At least one industry leader, the chairman of the East Coast Columbia Conference, was actually involved in litigation over the dual-rate issue. Although the congressional hope of avoiding further litigation about the validity of exclusive patronage contracts was realized as a result of the interim legislation, ever-alert lawyers found an issue in the meaning of the interim legislation. There is no rest for the wicked.

The chairman of the East Coast Columbia Conference petitioned the New York Supreme Court to compel two shippers to arbitrate a dispute with the conference over the obligations of a dual-rate exclusive patronage contract. The respondent shippers replied that the arbitration contract had not been approved by the Board, and the temporary legislation did not preserve its validity in the absence of express Board approval.33 The new legislation, it was argued,
could not reach back and validate what the Supreme Court had found invalid under Section 14 of the Act. The New York court held the contracts executed by the conference, including the arbitration clause, valid under the interim legislation, granted the chairman’s petition and directed the arbitration to proceed. Another industry leader testified in 1961 that “[f]or over three years the industry has been in a state of uncertainty, and trading conditions between the United States and the rest of the world have deteriorated as a result.”

During the same period the Board, with its own severe health problems, brought on by exposure to the criticisms of Congressman Emanuel Celler, chairman of the Antitrust Subcommittee (No. 5) of the House Committee on the Judiciary, had not been idle and began to consider long dormant dual-rate issues during this period. A complaint, which had been filed in 1953 by Isbrandtsen as a shipper of cotton and by four other cotton shippers identified with the Kempner cotton shipping interests, against States Marine, Lykes, Waterman and several other lines operating from the Gulf of Mexico to Japan and to Mediterranean ports was deemed ripe for decision. The issues in this proceeding were thought to be the same as those in the Japan-Atlantic Conference case—the validity of the dual-rate contract practice—possibly because of the fact that the carriers used exclusive patronage contracts and two rate levels, and because of the presence of the perennial maverick Isbrandtsen as a complainant. The complaints against the Far East Conference and the Gulf Mediterranean Ports Conference were that they used the dual-rate contract system in violation of the Act. Here too it was argued that the system was necessarily unlawful and that the conference lines could neither ask shippers to sign an invalid contract nor charge the higher of two rate levels because of its unlawfulness. Naturally the lower rate level

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34 Testimony by Mr. Wierda before the Merchant Marine and Fisheries Subcommittee of the Senate Commerce Committee, 87th Cong., 1st Sess. 100 (1961).
was thought to be the valid one. The facts in Isbrandtsen's case against the Japan-Atlantic Conference before the Supreme Court, and the facts before the Board in Isbrandtsen's case against the Far East and Mediterranean Conferences were quite different, however. The differences were that in the latter proceeding Isbrandtsen was a shipper and no outside or independent carrier competition with the conferences had been shown to exist. Isbrandtsen was so completely outside the trade it had to suffer the indignity of becoming a shipper. In the Supreme Court case Isbrandtsen was complaining as an independent carrier who was being harmed by the competitive tactics of the conference. As shippers, neither Isbrandtsen nor the Kempner interests produced any evidence of harmful competitive effects on other carriers, but relied instead on arguments that the system itself was invalid regardless of proof of competitive effect. Lack of proof on this critical point controlled the outcome of the case, as it should have. Another and important difference was that the shippers themselves had requested an exclusive patronage contract and two rate levels. The conferences did not initiate it for competitive reasons.

The Board recognized the absence of carrier competition and the presence of shipper solicitation as vital differences from the earlier proceeding when it held that the dual-rate contract system employed by the respondents was not being used as a competitive measure and was not shown to have been designed to meet outside competition, and therefore was lawful.\textsuperscript{6} The Board stated that past court

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\footnote{6} Isbrandtsen Co. v. States Marine Corp., 6 F.M.B. 422 (1961). The portions of the Board's order applicable to Isbrandtsen and States Marine were upheld, but Isbrandtsen was held to be entitled to interest on its reparation from the date of filing its complaint and not from the date of the Board's order. States Marine Lines, Inc., v. Federal Maritime Comm'n, 315 F.2d 906 (D.C. Cir. 1963). The Board's order applicable to Kempner and the Gulf Mediterranean Ports Conference was reversed and remanded for assessment of reparations. Kempner v. Federal Maritime Comm's, 313 F.2d 586 (D.C. Cir. 1963). The Kempner decision contains an unexplainable error of fact as a basis for the decision. The decision stated that the "discriminatory rates here involved were not approved by the regulatory agency . . . and were illegal." \textit{Id.} at 587. No rates were in evidence in the record, the Commission's report is silent as to rates, approval of the rates was not challenged by any party nor made an issue anywhere in the case and the approval of tariff rates was simply a non-existent factor in the case. Such...}

decisions dealing with the trade practice do not "declare the practice or system unauthorized under all circumstances" nor did the Supreme Court in the Isbrandtsein case set aside any Board orders insofar as they approve the exclusive patronage system as a general proposition, but only disapproved the particular use of the system by a conference in such a way as to injure an independent common carrier by water.\textsuperscript{37}

The complainants' adherence to the doctrinaire theory regarding the inherent invalidity of the dual-rate contract system must have led them to their relaxed position as to the lack of any need for facts showing competitive injury. The complainants must also have shared, ahead of time, the Senate Committee's predicted widespread confusion about the effect of the Supreme Court's 1958 holding,\textsuperscript{38} by not realizing that differences in proof would compel a different result. Eight days after the report in the Isbrandtsein-States Marine case, the Board's own health problems were resolved by the abolition of the patient and by the creation of a new five member Federal Maritime Commission.

The abolition of the Maritime Board, the Board's report in the Isbrandtsein-States Marine case which clarified the distinction between the trade practice of giving freight rate discounts to signers of exclusive patronage contracts and the terms of individual shippers' contracts, followed by new legislation which likewise embodies a recognition of differences between the permissibility of the trade practice and the standards for approving shippers' contracts, all in the Fall of 1961, should provide a fresh start on thinking about the future validity of the practice and should assuage many industry leaders' afflictions of recent years.

The failure to distinguish between the validity of the system as a generalized trade practice and the validity of

\textsuperscript{37} Isbrandtsein Co. v. States Marine Corp., \textit{supra} note 36.

\textsuperscript{38} The briefs and arguments in this case were prepared and delivered in 1956-1957.
specific terms of individual exclusive patronage contracts has been a source of much of the confusion and conflicting argument. In the *Isbrandtsen-States Marine* case the argument was made that since the practice or system was illegal, the exclusive patronage contract tendered to Isbrandtsen was necessarily illegal too without reference to its terms. One commentator makes a point of the fact that the Supreme Court in the most recent *Isbrandtsen* case upheld the distinction between the exclusive patronage contracts used around 1916 and those used today, and follows this observation by a reference to "the legality of dual rate systems" as a "burning issue" and recommends the "authorization of dual rate systems only as defensive weapons of conferences for the purpose of limiting...competition." 39 The representatives of the Department of Justice also invariably discuss the shippers' contracts and the operation of the system together, and the Supreme Court itself in the *Isbrandtsen* case first described the dual-rate contracts and then held that section 14 "strikes down dual rate systems" where certain conditions exist. 40 This sequence of ideas is a source of misunderstanding.

The approvability of an exclusive patronage contract should be on an individual basis through application of specific standards, whereas the approvability of a general system or trade practice should be governed by broad considerations of public policy, and each should be dealt with as a separate issue. The Act, as recently amended, makes the distinct standards quite clear by providing in section 14b for a procedure to obtain permission to use shippers' exclusive patronage contracts providing lower rates to signatories and for the application of specific standards of approvability.

The Shipping Act was amended to authorize lawful continuation of "any dual rate contract arrangement in use by the members of a conference" unless disapproved by the newly created Commission, and to authorize the Commission to "permit the use by any common carrier or

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conference of such carriers in foreign commerce of any contract . . . which provides lower rates to a shipper or consignee who agrees to give all or any fixed portion of his patronage to such carrier or conference of carriers unless the Commission finds that the contract, amendment or modification thereof will be detrimental to the commerce of the United States or contrary to the public interest, or unjustly discriminatory or unfair as between shippers, exporters, importers, or ports” provided the contract contains nine different types of provisions. Thus the new law eliminates the general condemnation or outlawry implications of the 1958 Isbrandtsen decision, and exclusive patronage contracts as a part of an arrangement or system of two rate levels are not now invalid under any circumstances, as long as the Commission gives permission to use them.\footnote{41} However, the validity of the trade practice of requiring exclusive patronage contracts under section 14, when certain competitive conditions exist, is not so clear.

The fact that the Commission must now make findings as to the effect of an exclusive patronage dual-rate contract system when it is initiated still leaves the eventual status of the practice in doubt because of the often expressed view that the “normal inherent intent of any dual-rate system is to exclude competition.”\footnote{42} If this assumption is ever proven, the Commission could not approve agreements even under the new law. All the new law gives is certain

\footnote{41}It has been stated that the new law “legalizes, subject to several limitations, the use of the so-called dual-rate systems. . . .” Statement by President Kennedy, Oct. 4, 1961. In its report on section 14b the House of Representatives stated that the section expressly authorizes “the use of dual-rate systems by conferences, irrespective of the presence or absence of non-conference competition.” H.R. Rep. No. 498, 87th Cong., 1st Sess. 7 (1961).

Before considering section 14b, the Commission’s predecessors had to review and pass on dual-rate agreements by virtue of section 15 as interpreted in Isbrandtsen Co. v. United States, 211 F.2d 51 (D.C. Cir.), cert. denied, 347 U.S. 990 (1954). See also River Plate & Brazil Conference v. Pressed Steel Car Co., 227 F.2d 60 (2d Cir. 1955); Pacific Westbound Conference v. Leval & Co., 201 Ore. 390, 269 P.2d 541, cert. denied, 348 U.S. 897 (1954).

preliminary presumptions of validity. We still do not
know what specific factors make “public interest.”

A review of the history of the exclusive patronage
contract should help to disclose what factors of public inter-
est created the trade practice of using the contract, and
whether they are such as to sustain “inherent intent” as-
sumptions of the invalidity theory. The history of con-
ferences and their uses of the exclusive patronage contract
with rate differentials suggests that the inherent intent
to stifle competition, the competitive measure, and the
retaliatory device notions are newcomers and that self-
preservation through the shipper-tie and advantages to
shippers through relatively unchanging rates and assured
service are the dominant incentives for using the system.
Much of the newly discovered proof of bad effects, as one
might suspect where such expressions as “necessarily,” “in-
herent” and “per se” are used, is argumentative, inferential
and not based on factual findings of damage to the public.

Exclusive patronage contracts between shippers and
ocean carriers are older than conferences and precede even
the use of rebates, which were the first shipper-conference
tying arrangements thought to have adverse effects on com-
petition. Rate differentials, or dual rates, between con-
tracting shippers and other shippers pursuant to rate
schedules are almost as early in time, having begun some
time after 1875, about the same time as conferences
originated.43 By 1906 the conference system and the con-
ference use of exclusive patronage contracts with shippers
was an established practice, and rate differentials, then
called discounts, were in use, although not in general use.
The rebate system was more generally used.44

Two significant conclusions emerge from the history
of shipping conferences: first, the use of exclusive patronage
contracts providing for less than tariff rates or rate dif-

43 The first conference between shipowners appears to have been organized
in 1875 and was known as the Calcutta Conference. It concerned the tea
trade between Calcutta and London.
44 The history and background for these practices has been reported in
the Report of the Royal Commission on Shipping Rings (1909).
Differentials was an established practice long before the Act in 1916, and existed at the time of the Act; second, the trade practice was brought about principally in response to demands of shippers. Competitive considerations were present, but the dominant competitive weapon was rate reductions rather than the contract. The intent and effect of the contract and two rate levels traditionally has not been to meet outside competition but to assist shippers. The conference agreements between carriers may have been designed primarily to dominate the competition and rate cutting to drive out competition, not the exclusive patronage contract nor the differential in freight rates.

Since this trade practice was so well known in American and British ocean commerce by 1916, it would have been anomalous for Congress in 1916 to outlaw the practice by inference rather than expressly as it did in the case of rebates. This conclusion has not only the support of history, but also the findings of a congressional committee and subsequent court decisions. The only remotely possible court qualification prior to the Isbrandtsen decision in 1958 was a Supreme Court decision in 1917 reversing a district court decision upholding a conference combination.45

Before legislative inquiry, the courts had reviewed conference combinations in England and found them to be consistent with the common law in Mogul Steamship Co. v. McGregor.46 In 1890, in the United States, public policy took a different direction with the enactment of the Sherman Anti-Trust Act.47 The Sherman Act, as originally enacted, made any combination in restraint of trade or commerce, including part of the trade or commerce with foreign nations, by any person a misdemeanor. This act defined person to include corporations and associations existing under the laws of any foreign country. The Supreme Court held that the law applied to all contracts tending to create a monopoly whether or not they are unlawful at common law.48 This

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46 23 L.R. 598.
48 United States v. Trans-Missouri Freight Ass'n, 166 U.S. 290 (1897).
seems to make the Sherman Act applicable to conference combinations. The applicability of the Sherman Act to steamship conferences and to their contracts did not receive judicial interpretation in the United States, although the case of United States v. Prince Line posed the issue. The purpose of the suit was to dissolve alleged unlawful combinations and to enjoin certain practices of the respective companies. With the exception of an injunction against certain discriminatory practices, the bills were dismissed. The district court upheld the conference combination including the use of the rebate although it conceded that the questions presented had become largely academic because of the advent of the First World War. On appeal to the Supreme Court the judgment was reversed, since war conditions had caused the cases to become moot and the Court was without power to review the issue on the merits.

In 1912, the Committee on Merchant Marine and Fisheries (commonly called the Alexander Committee) was directed to make a complete and thorough investigation of the methods and practices of the various shipping lines, both domestic and foreign, engaged in carrying our overseas or foreign commerce. The Committee was to investigate whether any such ship lines had formed any agreements among one another for the purpose of fixing rates and tariffs, or of giving and receiving rebates, special rates, or other special privileges or advantages, or for the purpose of pooling or dividing their earnings, losses or traffic, or for the purpose of preventing or destroying competition.

After making recommendations regarding the necessity for governmental scrutiny and approval of specified types of agreements the Committee proposed legislation which finally became the Shipping Act of 1916. The Committee's summary and recommendations indicate that while Congress was familiar with the practice of using exclusive

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50 Hearings Before the House Committe on Merchant Marine and Fisheries, 62d Cong., 2d Sess. 290 (1913).
patronage contracts with shippers and with the use of rate differentials, it regarded conference agreements and rebate clauses and practices as something distinct from such contracts. Current efforts to lump all these practices together and to make them all subject to the Act’s prohibitions are out of place. Only the two practices mentioned were the principal subjects of investigation and of the legislation that resulted. The Committee considered exclusive patronage contracts as not against public policy and that they were an accepted trade practice neither requiring extensive inquiry nor legislative action.

It is not surprising then that exclusive patronage contracts and rate differentials as conference trade arrangements have not been completely invalidated. Certain aspects of the arrangement such as excessive rate differentials have been invalidated because they were arbitrarily selected or were undue or unreasonable. The administrative procedures or formality of approval under Section 15 of the Act have been declared improper, and the Shipping Board has condemned the arrangement where it operates solely to effect a monopoly, but the trade practice as such had never been declared invalid per se until the circuit court so held in the Isbrandtsen case.

Up to this point and until 1958, a period of about eighty-three years following the formation of the first shipping conference in 1875, exclusive patronage contracts had sur-

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53 Swayne & Hoyt Ltd. v. United States, 300 U.S. 297 (1937).
55 Eden Mining Co. v. Bluefields Fruit S.S. Co., 1 U.S.S.B. 41 (1922). The Eden case is the first case in which the dual-rate question was presented to a predecessor of the Commission for determination of legality under the Act. It was held to be a violation both of section 16 and section 17 to have an exclusive patronage contract providing for a more favorable rate for contract shippers than for non-contract shippers. The second case was Rawleigh v. Stoomvaart, 1 U.S.S.B. 285 (1933). The Rawleigh case distinguished the Eden case as involving a single carrier monopolizing the trade in comparison with conference dual-rate systems which are established by several carriers.
vived legislative inquiry and judicial scrutiny in both Great Britain and America without being found to be a retaliatory device and, as such, sufficiently contrary to public policy to justify remedial legislation or adverse court order through interpretation of existing legislation.

The history of the trade practice does not conflict with the Committee's findings and suggests that unless it has undergone drastic modification since then, or unless the contracts have become unduly oppressive, restrictive legislation is still not justified. The exclusive patronage contract and discounts are still regarded as an accommodation to shippers desiring relatively unchanging rate conditions. There is no intent to retaliate or to stifle competition in such a situation, but only to assure the lines of a steady flow of cargoes and income to support regular departures, and to help shippers to make forward booking contracts with reasonable assurance that delivery prices will not change much in the meantime. The shippers who are a mainstay of the trade want a lower rate than those who are not.

The shippers' tie also became important to the preservation of the conference system later, as well as an aid to shippers, rather than a device to kill off antagonists. The former chairman of the Federal Maritime Commission has expressed this cogently in testimony before a congressional committee:

We further believe that if the conferences are to be continued they must have the power to assure themselves the loyalty of merchants upon whose trade they depend. It is our belief that the only workable method of achieving such purpose and which is not at the same time contrary to the American concept of fairness is the dual-rate system. . . . We believe that the exclusive patronage system appropriately regulated to insure fairness between the shipper or consignee on the one hand, and the carriers on the other, is the proper instrument. . . . 57

Even so, competition is a factor, although not a dominant one, since it is probably not possible to have an exclusive

57 Testimony of Mr. Stakem, quoted in Hearings Before the Special Subcommittee on Steamship Conferences of the House Committee on Merchant Marine and Fisheries, supra note 42, at 24.
patronage contract that does not exclude outside carriers from the reservoir of cargoes controlled by contract shippers and to the extent of the exclusion it will tend to hurt non-conference carriers.\textsuperscript{58}

The successful evolution of the exclusive patronage contract practice and of federal legislation protecting the practice has been accomplished only after a series of court decisions turning back challenges to its validity. The challenges prominently supported by the Department of Justice have brought about, over the years, consistent court support of the underlying public policy favoring a regulated exclusive patronage contract system.

In the first of the court challenges, \textit{United States Navigation Co. v. Cunard S.S. Co.},\textsuperscript{59} a plaintiff sought to enjoin the defendant steamship lines from using the system of contracts and rates on the ground that it violated the Sherman Anti-trust Act and the Clayton Anti-trust Act. Dismissal of the complaint was affirmed on the ground that the Shipping Act covers the dominant facts alleged as constituting a violation of the anti-trust laws, particularly Section 14 of the Act which prohibits retaliation by common carriers by water against a shipper by resorting to discriminatory or unfair methods.\textsuperscript{60} If the practice were illegal under any circumstances or because of its inherent defects, as claimed, the dismissal because of the administrative agency's primary jurisdiction would have been a useless action and the Court should have passed on the defects then and there. The Court must have thought more facts showing bad competitive effects had to be produced before it could pass judgment. None were shown. The second challenge came on an appeal from an order of the Secretary of Commerce enjoining the use of exclusive patronage contract systems in intercoastal trade.\textsuperscript{61} As the Secretary interpreted the evidence before him, the operation of the

\textsuperscript{58} See Testimony of Mr. James, quoted in \textit{Hearings Before the Special Subcommittee on Steamship Conferences of the House Committee on Merchant Marine and Fisheries}, supra note 42, at 125.

\textsuperscript{59} 284 U.S. 474 (1932).

\textsuperscript{60} Id. at 483-84.

\textsuperscript{61} Swayne & Hoyt Ltd. v. United States, supra note 53.
system would not differ substantially from deferred rebates which were expressly outlawed by Section 14 of the Act in both foreign and coastwise shipping. The Court stated in its opinion: "Even though, as appellants seem to argue, the evidence may lend itself to support a different inference, we are without authority to substitute our judgment for that of the Secretary that the discrimination was unreasonable." Both rebating and unreasonable discrimination resulting from the way the practice was used, rather than illegality under any circumstance, were the basis of the decision, so this case is not authority for the conclusion that any exclusive patronage contract and two rate system is unlawful.

The facts in a third challenge showed that the North Atlantic Continental Freight Conference "sent notices to all known shippers in the North Atlantic trade that effective November 1948, the exclusive patronage contract—non-contract rate system would be inaugurated and that shippers who refused to enter into contracts to ship with the conference lines exclusively when they could provide transportation were to be charged 20 per cent to 30 per cent higher than the contract rates." The Board dismissed a complaint alleging illegality in such action even though an examiner had found the differential had been arbitrarily selected. Isbrandtsen, the Attorney General and the Secretary of Agriculture contended, before the district court, that a dual-rate provision in a conference agreement was, in all circumstances, invalid under Section 14 of the Act. The court's decision stated that "for the purposes of this decision we assume that, as the Board contends, under some circumstances the Board may, pursuant to 46 U.S.C.A. § 814 (section 14) approve a conference agreement containing such a provision." The court, however, set aside

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62 Id. at 307.
65 Id. at 885-86.
the Board's order and enjoined the conference from using
the dual-rate provision on the ground that the 20 per cent
to 30 per cent differential had been arbitrarily selected.
The rate differential, not the practice, was invalid here.
A fourth challenge came when the federal government,
instead of a shipper, acting by the Attorney General brought
suit against the Far East Conference under the Sherman
Act to enjoin the defendants from using the exclusive
patronage contract system.\textsuperscript{66} The fact that the government
and not a shipper was the complainant was held to be
immaterial as long as the Board was the expert agency
responsible for administering the Act, and administrative
remedies dispensed by the Board had to be sought and
pursued to a final conclusion before resort may be had
to the courts.\textsuperscript{67} Again the Court refused to hold that the
contract rate system was unlawful under any circumstances.
Up to this point, the law established by these cases was
that: (1) a complaint charging illegality of an exclusive
patronage contract dual-rate system will be dismissed unless
the acts charged have been reviewed by the Commission as
an administrative agency having jurisdiction to administer
the Act; (2) where the use of the system had been found
administratively to operate in a way not differing sub-
stantially from expressly prohibited acts, the courts will not
overrule a finding of illegality; and (3) if the differentials
between rate levels used by a conference in connection with
an exclusive patronage contract system are arbitrarily
selected (i.e., without a study of the needs of the trade),
the practice may be enjoined.

The fifth and last challenge to the practice in \textit{Federal
Maritime Bd. v. Isbrandtsen Co.},\textsuperscript{68} has left us with a
fourth principle to the effect that a practice of asking dual
rates for exclusive patronage contracts, adopted for the
purpose of curtailing competition, and a practice of using
a contract which contains provisions tying shippers in such

\textsuperscript{67} \textit{Id.} at 576.
\textsuperscript{68} 356 U.S. 481 (1958).
a way as to have the effect of stifling outside competition must both be held unlawful.

The Department of Justice inferred from roughly the same background of history that the trade practices and contracts at the time of the Alexander Committee's investigations from 1913 to 1916 leading to the enactment of the Act were not comparable to what now exists. Unquestionably the terms of the contracts have changed over the years, but the practice of using them is essentially the same. The historical evidence thus disputed is inconclusive as to the extent to which the contracts were used, and as to whether they were the exception rather than the rule.

The historical background of dual-rate exclusive patronage contracts plus congressional action to stop litigation that would extend the Isbrandtsen decision by invalidating all exclusive patronage systems, followed by legislation expressly authorizing the Commission to permit use of exclusive patronage and dual-rate systems, should convince that the practice is not inherently, or per se, contrary to the public interest or detrimental to commerce. The reporting committee on the new section 14b legislation vouchedsafed this conclusion when it stated that the new law expressly authorizes "the use of dual-rate systems by conferences, irrespective of the presence or absence of non-conference competition." The automatic equation between the practice and retaliation alleged to exist under Section 14 of the Act is not proven and the Department's efforts to get the courts to use this theorem have failed. Nevertheless, in the face of (1) the long sustained hostility of the Department and its interpretation of the evidence regarding early use and the traditional purposes of the practice, (2) the Isbrandtsen interpretation of the retaliation provisions of section 14 where competition and rate cutting are proven, and (3) the possibility that the new Commission may still view dual-rate systems as a competitive measure

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and as a retaliatory action where it coincides in time with rate cutting, it would take a courageous lawyer to tell his client that the status of the practice has been settled favorably to a return to old practices because of the new legislation. What then can one tell a client? First, before an exclusive patronage system may be followed, after April 3, 1964, an express declaration of permission by the Commission will be essential; second, the permission may be forthcoming only if the request for permission is sought when competition by a non-conference operator is present, and the practice will only be used as a defensive measure. It is the thesis of this article, however, that the latter would be an erroneous standard and, if the necessary competitive measure standard is followed, the courts will very likely invalidate the use of the contract system because a defensive measure seems also to be regarded by the courts as necessarily coercive. The middle or competitive necessity ground in this case is fraught with danger since the best defense against a rate war is to render the non-conforming carrier's competition uneconomic, using the superior coercive economic power of the conference lines. The true intent of the latest Isbrandtsen decision seems to nullify the excuse of controlling rate wars or off-setting non-conference competition as a valid purpose for exclusive patronage contract systems. To some extent any response to the activity of an independent line is retaliation. The new legislation does not resolve the problem of evaluating competitive impact.

The most the new legislation does, as far as permitting the use of contracts that provide lower rates to shippers who give their patronage to a carrier, is to place the burden of proving detriments to commerce, contrariety with public interest, discrimination, unfairness and the like on persons who oppose the permission. The Isbrandtsen decision, holding arrangements which stifle independent competition retaliatory and thus violative of section 14, is still the law, and if this is shown in any case the arrangement would be struck down.

Steamship conference activity exists in a context of competition, of course, and a program of requiring shippers to sign exclusive patronage dual-rate contracts is a vital part of this activity. As a matter of fact, such a program is usually initiated with reference to competition by independent lines when it becomes no longer possible to quote firm rates from week to week, and rates begin to change rapidly. The Maritime Commission is charged with the duty of striking a balance of allowable impact on the competition of independents. The Commission's job may be eased because it does not have to prove that the law of the Isbrandtsen case is inapplicable in the context of the facts surrounding any specific application for permission, but a basic source of difficulty in validating contract systems under the new law is still with us. These are the conflicting inferences drawn from certain past practices, or even that they exist as traditional practices as this article has sought to establish, and whether in any particular situation independent competition is being stifled by retaliation and shippers deprived of a choice of carriers because of the exclusionary aspects of the contracts' provisions or as the result of their rigorous damage clauses. The report of the Anti-trust Subcommittee on March 1, 1962, doubts that the evidence shows the contracts to be in the public interest:

Upon consideration of all the testimony at our hearings and upon weighing the detrimental effects of dual-rate contracts on domestic shippers, importers, independent lines, and upon the commerce of the United States which, when taken together, are not insubstantial, against the few benefits said [but not proved] to be derived from dual-rate agreements, the subcommittee tends to concur in the privately articulated views of some industry spokesmen that a factual case for dual rates has not been made.72

This article tries to show there is considerable evidence that the trade practice need not operate destructively as a retaliatory competitive measure, although it may be misused for this purpose, but more evidence of past usage of the contracts and of their terms is needed for any conclusive

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judgment about the purposes of conferences in tendering contracts to shippers and in promulgating two-level tariffs. A trade practice of long and historical standing should not be invalidated except on the clearest proof of public injury and changed circumstances. Detailed historical facts about the practice and the effects of the exclusion are meagre, so it might be well to have a moratorium on arguments until this course of legal bickering over necessary inferences is removed by finding out more about the origin, development, use and effect of the practice. With such information the courts and the Commission might be able to decide where the practice stands in relation to the enforcement of the Act and to our public policy about undue restraints on competition. Objective tests may also be discovered against which contract systems can be compared to determine conformity with "detrimental to commerce" or "public interest" standards of section 14b.

The Department of Justice draws inferences from the fact that in the past the practice was an exception. Other writers believe the practice can be justified only as a defensive measure. This writer believes it is a valid practice by virtue of historical acceptance and the burden is on those who challenge to show invalidity.

The time may be at hand in the international shipping industry where we must pass from sterile arguments about whether a practice is necessarily coercive or unlawful per se because of ill-defined overtones of national policy expressed in the anti-trust laws, into the real world of actual business needs in international ocean commerce. The facts of modern day ocean commerce and long-established international shipping usages should be marshalled to find out just what kind of freedom is needed before presently undefined statutory standards of public interest can be applied to invalidate the practices and the implementing contracts used by carriers.

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