

‘Nervine’ and Knavery:
The Life and Times of *Dr. Miles Medical Company*

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... *for nervousness or nervous exhaustion, sleeplessness, hysteria, headache, neuralgia, backache, pain, epilepsy, spasms, fits, and St. Vitus' dance.*
Dr. Miles ‘Restorative Nervine’ Label

I cannot believe that in the long run the public will profit by this court permitting knaves to cut reasonable prices for some ulterior purpose.
Justice Oliver Wendell Holmes, Jr.

Introduction

In the spring of 1911, the Supreme Court issued four opinions involving the Sherman Act, all of them landmark decisions and each in its own way reflective of the era. The *Standard Oil* and *American Tobacco* decisions affirmed dissolution of the notorious oil and tobacco trusts, the first controlled by John D. Rockefeller and the latter by J. B. Duke. The cases confirmed federal power to impose a regime of competition in the public interest. The Court adopted a rule of reason that would later resolve into the microeconomic logic of modern antitrust analysis. In *Gompers*, the Court sanctioned the issuance of contempt citations to enforce the judicial practice of enjoining labor union strikes. Three years later, Congress would pass the Clayton Act in an effort to limit the broad judicial discretion seen in the rule of reason and to curb the widespread use of injunctions against labor unions.¹

The fourth decision was *Dr. Miles Medical Company v. John D. Park & Sons*. Justice Charles Evans Hughes, writing for the Court, not only pronounced the doctrine that resale price maintenance was *per se* illegal (without recourse to Latinate diction) but set in motion the analytical dynamics of modern vertical restraints doctrine.² Moreover, the underlying controversy offers a striking vignette of the era’s swirling cultural and economic currents. *Dr. Miles* arose at the confluence of three federal statutes emblematic of Progressive Era responses to entrepreneurial excess. As every antitrust student knows, the Sherman Act grounded Park’s successful defense that the resale price provisions in Miles’ form contract were unenforceable.

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¹ *Standard Oil Co. v. United States*, 221 U.S. 1 (1911); *United States v. American Tobacco Co.*, 221 U.S. 106 (1911); *Gompers v. Buck's Stove & Range Co.*, 221 U.S. 418 (1911) (holding criminal sanctions for contempt improperly issued but inherently part of court powers in proper proceedings). Clayton Act of 1914, ch. 323, 38 Stat. 730 (current version at 15 U.S.C. § 18 (2006)). For a description of that era, see RUDOLPH J.R. PERITZ, *COMPETITION POLICY IN AMERICA: HISTORY, RHETORIC, LAW* at Chs. 1 & 2 (2001) (hereinafter PERITZ, *COMPETITION POLICY*).

² *Dr. Miles Medical Co. v. John D. Park & Sons Co.*, 220 U.S. 373 (1911); Peritz, *A Genealogy of Vertical Restraints*, 40 HASTINGS L.J. 511 (1989) (hereinafter Peritz, *Genealogy*); *State Oil v. Khan*, 522 U.S. 3 (1997) (applying rule of reason to maximum resale price maintenance). See *Leegin Creative Leather Products, Inc. v. PSKS, Inc.*, 2006 WL 690946 (5th Cir. 2006) (minimum resale price maintenance illegal *per se*), 2006 WL 2466835 (Justice Scalia granting stay pending decision on petition for writ of certiorari).

The context was also framed by the Trademark Act of 1905³ and the Pure Food & Drug Act of 1906,⁴ both of which collided with the dominant marketing strategies of patent medicine firms. Because the costs of market entry and product imitation were low, supply tended to exceed demand, spurring intense brand competition.⁵ But the trademark statute's stronger protection of nationwide brands in the patent medicine industry, the first market driven by mass advertising, enabled large manufacturers to distance themselves from smaller firms and discourage upstarts.⁶ Moreover, the food and drug act's ingredient disclosure requirements and its ban on ill-founded therapeutic claims tended to benefit well-established firms as much as consumers.⁷

The chapter's first section describes the era's patent medicine markets and pays close attention to the commercial importance of trademarks and advertising. In this light, the second section analyzes *Dr. Miles* through the prism of prior litigation in the industry, an analysis that uncovers the centrality of property rights in the Court's competition policy. That policy is misunderstood today, particularly its underlying classical economics, which informed the twin common law competition doctrines of contracts in restraint of trade and restraints on alienation of property. The chapter concludes with an afterword about modern vertical restraints doctrine and its common law underpinnings.

I. Patent Medicine Markets in the Progressive Era

The term "patent medicine" was largely a misnomer. Very few of them were actually patented.⁸ The vast majority – whether celery bitters, sarsaparilla tonics or bone liniments – boasted the therapeutic value of secret ingredients and thus were more accurately called proprietary medicines. A number of today's mouthwashes, cough syrups and cold medications began as patent medicines and retain their brand popularity as well as their core ingredient – alcohol. Other products that began as patent medicines have migrated to twenty-first century kitchens: The vegetarian cure first known as "Dr. Miles' Compound Extract of Tomato" is likely taken from bottles labeled HEINZ KETCHUP.⁹ COCA COLA contained narcotic cocaine

³ Act of Feb. 20, 1905, ch. 592, § 5, 33 Stat. 724. The prior Trademark Act of 1871, ch. 230, 16 Stat. 198, was declared unconstitutional in *United States v. Steffens*, 100 U.S. 82, 97 (1879).

⁴ Pure Food and Drug Act of 1906, Pub. L. No. 59-384, 34 Stat. 768, 768-70 (repealed 1938).

⁵ JAMES YOUNG, *THE TOADSTOOL MILLIONAIRES* 165-66 (1961) (hereinafter *TOADSTOOL*).

⁶ On rising economies of scale in not only production and distribution but advertising, see ALFRED CHANDLER, JR., *SCALE AND SCOPE: THE DYNAMICS OF INDUSTRIAL CAPITALISM* 63-65, 168-70 (1990).

⁷ See, e.g., Susan Foote & Robert Berlin, *Can Regulation Be as Innovative as Science and Technology? The FDA's Regulation of Combination Products*, 6 *MINN. J. L. SCI. & TECH.* 619, 624 (2005). Market participants practiced highly sophisticated forms of product differentiation long before economists developed the tools to describe and analyze them. See generally, PERITZ, *COMPETITION POLICY* at 106-110; Peritz, *Dynamic Efficiency*, in *POST-CHICAGO DEVELOPMENTS IN ANTITRUST LAW* 108 (2002) (Cuccinota, A., et al, eds.).

⁸ In 1796 the first and one of the few actual patents for a patent medicine was issued to a Dr. Samuel Lee for his "Bilious Pills." *TOADSTOOL* at 31-35. Patents were more often issued for therapeutic devices. The first was issued in 1796 to a Dr. Elisha Perkins, a founder of the Connecticut Medical Society, for "Metallic Tractors," which were recommended for "Rheumatism, Pleurisy, Some Gouty Affections, etc., etc." *TOADSTOOL* at 21-27; STEWART HOLBROOK, *THE GOLDEN AGE OF QUACKERY* 34-36 (1959) (hereinafter *QUACKERY*).

⁹ *TOADSTOOL* at 171; DAVID ARMSTRONG AND ELIZABETH ARMSTRONG, *THE GREAT AMERICAN MEDICINE SHOW* 167 (1991). (hereinafter *MEDICINE SHOW*).

until 1903 and was advertised as a “brain tonic and intellectual beverage” under the name of “Beverage Moxie Nerve Food.”¹⁰

The predominant business strategy for patent medicine makers involved not patents but trade secrecy, intended to conceal the identity of ingredients from both rivals and customers. Relentless advertising of trademarked names and images sought success in overcrowded and highly contested markets. This volatile mixture of secrecy and publicity, catalyzed by low production costs, yielded differentiated product markets rampant with multiple asymmetries of product information, market failures that improved conditions for widespread entrepreneurial excesses that often bordered on fraud. The section describes those markets by plotting the product and demographic dimensions of differentiation. Thereafter, the section turns to congressional legislation that can be understood in retrospect as Progressive Era responses to correct the informational asymmetries resulting from the business model of trade secrecy and trademark publicity. The *Dr. Miles* case resolved questions of competition policy and property rights in these cultural, economic and legal circumstances.

A. Highly Differentiated Markets

Proprietary medicine brands such as DR. HARTMAN’S PERUNA, KICKAPOO INDIAN COUGH CURE, and LLOYD’S COCAINE TOOTHACHE DROPS were just as recognizable to consumers a century ago as their modern counterparts – VICKS NYQUIL, ROBITUSSIN, and BAYER aspirin – are today. The ante-bellum period saw a sharp rise in consumption of patent medicines that has been attributed to several factors, including distrust and short supply of doctors, self-medication as a reflection of American individualism, and thinly veiled alcohol and narcotic use in an era of increasing pressure for temperance.¹¹

Production and consumption profiles reflected intense product differentiation in two dimensions: product flavors and ingredients; and consumer demographics, particularly along gender lines. As one historian observed:

[T]he big-scale patent medicine maker . . . blazed a merchandizing trail. He was the first American manufacturer to seek out a national market. . . . the first producer to help merchants who retailed his wares by going directly to consumers with a message about the product. . . . the first promoter to test out a multitude of psychological lures by which people might be enticed to buy his wares. While other advertising in the press was drab, his was vivid¹²

The combinations and permutations of purportedly therapeutic agents were endless. And the flavors were myriad. Some recipes used sarsaparilla or cherry, others swamp root or celery teas. They were sweetened with molasses, soured with vinegar, or braced with bitters. Whatever the

¹⁰ MEDICINE SHOW at 161; JAMES GRAY, WHY OUR DRUG LAWS HAVE FAILED AND WHAT WE CAN DO ABOUT IT 21 (2001)

¹¹ Cf. QUACKERY at 15-17 (“Temperance Drinkers”); TOADSTOOL at 165; Joseph Kennedy, *Drug Wars in Black and White*, 66 LAW & CONTEMP. PROBS. 153, 160 (2003).

¹² JAMES YOUNG, THE MEDICAL MESSIAHS 21 (1974).

mix, most patent medicines began with alcohol or an opiate, although LUNGARDIA started with turpentine and kerosene, while TUBERCULENE contained creosote.¹³ DR. BATEMAN'S PECTORAL DROPS, a popular choice since the revolutionary war era, contained laudanum – both opium and alcohol.¹⁴ Federal law did not ban most opiates until the second decade of the twentieth century, allowing BAYER and JAMES SOOTHING SYRUP, among others, to sell heroin as a pain killer over-the-counter.¹⁵

Production costs were low. One reliable estimate put the cost of a dollar bottle of PERUNA, the period's most popular patent medicine, at fifteen to twenty cents.¹⁶ Because manufacturing costs were low and new-fangled recipes easily concocted, the patent medicine market was enticing to would-be entrepreneurs. According to one observer, their number was as "formidable . . . as were the frogs of Egypt." A prominent trade journal listed more than 28,000 nostrums in 1905. The great majority of producers were small struggling firms. The large manufacturers, like their contemporaries in other sectors of intense competition, sought to consolidate their market positions. But their vehicle was not merger or outright cartel. It was the Proprietary Association, founded in 1881. A. R. Beardsley, treasurer of Dr. Miles Medical, was an active and influential leader of the Association, which protected the interests of large manufacturers by lobbying at both state and federal levels, drafting standard form contracts for newspaper advertising and for product distribution, and coordinating efforts to protect trademarks and maintain retail prices.¹⁷

In the crowded patent medicine business the most significant cost was marketing. Whatever the chosen ingredients or the favored channels of advertising, success in product differentiation depended upon establishing a distinctive trademark, which was "the fixed star in a universe of flux":

The ownership of medicines might change again and again, and so might the formulas. The diseases for which medicines were advertised might vary over time, and sometimes even names were altered. Trade-marks, however, . . . endured forever.¹⁸

No trademark was more recognizable than the figure of LYDIA PINKHAM, whose marketers were confident enough to make public the ingredients for her Vegetable Compound long before the Pure Food and Drug Act of 1906 required it. Nor was there a brand with stronger customer loyalty than PERUNA, though its steps were dogged by P-RU-NA, PERINA,

¹³ ANN ANDERSON, SNAKE OIL, HUSTLERS AND HAMBONES 29 (2000). The raw petroleum contaminating someone's salt wells was sold as "The Most Wonderful Remedy Ever Discovered." TOADSTOOL at 171.

¹⁴ Three popular patent medicines were found to have a range of alcoholic content: HOSTETTER'S STOMACH BITTERS (44%), HARTMAN'S PERUNA (28%), PINKHAM'S VEGETABLE COMPOUND (18%). Samuel Adams, *Peruna and the Bracers*, COLLIER'S WEEKLY, Oct. 28, 1905, one of Adams' ten widely read and influential exposés, available at http://www.bottlebooks.com/Peruna_reprinted_from_collier.htm. TOADSTOOL at 129-30, 220-21; QUACKERY at 56, 85-87, 98-100, 110; MEDICINE SHOW at 167-69.

¹⁵ Harrison Act of 1914, ch. 1, 38 Stat. 785.

¹⁶ Adams, *supra* note 14.

¹⁷ TOADSTOOL at 109, 238. See discussion *infra* Part II. Regarding trade associations, see PERITZ, COMPETITION POLICY at 62-63, 75-78.

¹⁸ TOADSTOOL at 167.

ANUREP and other pretenders loosed by the period's weaker trademark protection. But few customers switched to PERUNA sound-alikes or to PINKHAM "generics," at least in part because the first movers did not rest on their laurels. The leading firms recognized, as did their rivals, that brand strength was brittle and depended on continuing efforts to bolster distinctiveness. In the decades bracketing the turn of the twentieth century, PINKHAM's annual advertising budget exceeded one million dollars. And no patent medicine maker bought as much newspaper columnage as PERUNA.¹⁹ On those efforts PERUNA for decades reigned as the most popular brand and the PINKHAM visage was as recognizable as those of Teddy Roosevelt and John D. Rockefeller.

While PERUNA gained a wide following largely through newspaper and circular advertising, PINKHAM early aimed its marketing at women and, it seems, at men who worried about them. One of its initial advertisements read:

A FEARFUL TRAGEDY, a Clergyman of Stratford, Connecticut, KILLED BY HIS OWN WIFE, Insanity Brought on by 16 Years of Suffering with FEMALE COMPLAINTS THE CAUSE. Lydia E. Pinkham's Vegetable Compound, The Sure Cure for These Complaints, Would Have Prevented the Direful Deed.²⁰

But it was not long before PINKHAM's advertising adopted a softer tone, most effectively in an informational pamphlet entitled *Guide for Women*, which described in plain language female physiology and disorders. It was distributed to drugstores and then door-to-door, first in Boston and in time nationwide. By 1901 the pamphlet had grown into a sixty-two page booklet. A successful national marketing program would subsequently include newspaper advertising but the foundation remained her *Guide*. For many years Pinkham's death remained secret and answers to questions from loyal readers continued to bear her name – until her demise was publicized in *The Great American Fraud*, COLLIERS WEEKLY's series of articles about the patent medicine industry that helped stir Congress to pass the Pure Food and Drug Act.²¹

Many other patent remedies were also aimed at women. They were successful, some scholars have suggested, because they supplied alcohol or narcotics to women who shied away from taverns in light of an emerging middle-class code of proper conduct. One category of patent medicines was bitters, which effectively flavored large doses of alcohol. Another product category was catarrh, which typically contained cocaine. There are estimates that by 1885 over seventy per cent of those addicted to opiates were middle-class and upper-class white women who had purchased the drug legally.²²

Of course there were special nostrums for "Secret Diseases of Men." In the Midwestern states, a large chain of medical institutes offered a "Wonderful Prolongation of the Attributes of Manhood." For those who could not afford the entire treatment, there was "Dr. Raphael's

¹⁹ TOADSTOOL at 104; QUACKERY at 96.

²⁰ QUACKERY at 60.

²¹ *Id.* at 62-65.

²² TOADSTOOL at 221. At the time, the overall rate of addiction was almost five persons per thousand, compared with the more recent rate of about two persons per thousand. HUMBERTO FERNANDEZ, HEROIN 20 (1998).

Cordial Invigorant” or from Armour & Company, the Chicago slaughter house and meat packer, there was “Orchis Extract,” advertised as the “Greatest Known Treatment for Weak Men,” and, from parts unknown, the exotic but hardly less subtle “Dr. Crane’s Turkish Wafers For Men Only / Turkish Method / The Sultans / and Harems.”²³

Medical institutes were not limited to the diseases of men. In 1890, for example, Dr. Miles opened his “Grand Dispensary” in Elkhart, Indiana, to join a growing number of medical infirmaries offering free advice, often through the mails, while selling patent remedies. Miles had begun publishing his free *Medical News* a few years earlier. Though the publication’s subject matter was not limited to women’s maladies, the era’s most successful product for Dr. Miles became “Restorative Nervine” on the promise of relief from “hysteria, blues, melancholy.” “Typical” advertisements in 1906 for the cure were aimed at its “large female following.”²⁴

Trademark familiarity and, with it, successful brand development were often built upon the mass distribution of gift publications that informed, advised or entertained – hand outs such as calendars, almanacs and books.²⁵ Repetition for brand recognition in mass markets, whether national or regional, required significant expenditures. James C. Ayer, for example, called attention to AYER CHERRY PECTORAL in his *American Almanac*, printed in his own publishing plant. By 1900, Ayer was spending an average of \$120,000 annually to print 16 million copies in 21 languages.²⁶ Dr. Miles was another of the period’s leading firms that published its own materials. In that time period, it spent in the neighborhood of \$200,000 annually on advertising and printed 6.5 million almanacs in addition to its calendars and “Little Books” series.²⁷

Patent medicine marketers also inundated urban markets with flyers and press advertisements. Some of the larger manufacturers, including Miles, reduced their advertising costs by using their presses to print local newspapers in exchange for advertising space. Indeed, Miles centennial biography would characterize the old firm as “more pressmen than chemists.”²⁸

Brand recognition was promoted through endless advertising – whether splashed across rural barns or crammed into the columns of metropolitan news dailies. Although roadway signage and building broadsides were condemned as despoiling the landscape, newspaper advertising most provoked critics and reformers. It was not just the volume and character of the

²³ QUACKERY at 69-84; TOADSTOOL at 175, 200-01.

²⁴ WILLIAM CRAY, MILES: A CENTENNIAL HISTORY 7, 24 (1984). Congress would pass legislation to prohibit mail-order medical treatment in 1922. *Id.* at 33.

²⁵ Traveling medicine shows were long the advertising medium of choice in rural areas until Rural Free Delivery became an official postal service in 1902, bringing mail order catalogues to the countryside. Parcel post service was introduced in 1913, giving rise to mail order houses. Magaera Harris, *Postal Service, in A HISTORICAL GUIDE TO THE U.S. GOVERNMENT* 469 (George Kurian, ed. 1998). The 1906 Sears catalogue included twenty pages of patent medicines. QUACKERY at 6.

²⁶ TOADSTOOL at 140-42.

²⁷ MARTHA PICKRELL, DR. MILES 48, 56 (1997); CRAY, *supra* note 26, at 19-21. The number of almanacs would reach 16.5 million in 1930. *Id.*

²⁸ *Id.*

ads. As newspapers and magazines came to depend on patent medicines for their primary source of advertising revenue, the advertisers began to assert their economic power over the press to make demands that corrupted editorial independence.

The most insidious example of corruption was the “red clause” in standard advertising contracts. The claret-inked clause voided the contract “if any law is enacted by your State restricting or prohibiting the manufacture or sale of proprietary medicines.” At a meeting of the Proprietary Association, a leading member confidently announced that the clause was “pretty near a sure thing.” And he was right. They were effective.²⁹ When state legislatures considered bills inimical to the patent medicine industry, editors, upon receiving letters that merely referred to these “muzzle-clauses,” would print articles or editorials supporting the industry. In fact, the Proprietary Association credited its many successes in quashing reform legislation to aid from the American Newspaper Association as well as individual papers. Even more egregious were the standard contract clauses that brazenly took a direct approach with provisions calling for cancellation if any detrimental matter “is permitted to appear in the reading columns or elsewhere in the paper.” Too often the result was either silence or praise of patent medicines.³⁰

Few newspapers and magazines dared run articles critical of their benefactors, despite growing concern among physicians, including the American Medical Association, and agitation by progressive reformers. For example, only one newspaper, the *Springfield Republican*, even reported on debate in the Massachusetts legislature over a labeling bill. By the 1890s, the *Chicago Tribune*, *New York Post* and a only few others reported patent medicine abuses; even fewer refused their advertising. The *Ladies’ Home Journal* in 1904 was the first popular periodical to take a step beyond occasional exposés and critiques when it launched a full-fledged campaign against the patent medicine industry. *Colliers Weekly* soon followed with ten articles by Samuel Hopkins Adams, entitled “The Great American Fraud.” The series remains the gold standard for investigative journalism calling for legal reform. Its tone of social and moral disapproval is captured in a still-renowned cover cartoon entitled “Death’s Laboratory.” The cover displays a skull with patent medicine bottles for teeth and an inscription on the forehead that reads “The patent medicine trust / palatable poison for the poor.”³¹ Each article focused on specific companies and products, in total attacking well over two hundred firms and individuals. The article that most provoked public outrage reported that the coroner in Cincinnati, Ohio, determined the death of a two-year old child was caused “by the poisonous effects of opium [in] a bottle of DR. BULL’S COUGH SYRUP.”³² The pure food and drug act was still over the horizon, and the label did not list ingredients.

B. Federal Legislation: Progressive Era Responses to Informational Asymmetries

²⁹ TOADSTOOL at 173, 205-25; QUACKERY at 1-41, 242-43; MEDICINE SHOW at 167-69.

³⁰ Mark Sullivan, *The Patent Medicine Conspiracy Against Freedom of the Press*, in THE MUCKRAKERS 182-87, 189-91 (Arthur Weinberg et al., eds., 1961). Cf. Edwin Baker, *Advertising and a Democratic Press*, 140 U. PENN. L.R. 2097 (1992).

³¹ See sources cited *supra* note 35; <http://www.fda.gov/cder/about/history/Gallery/galleryintro.htm> (cartoon); <http://www.mtn.org/quack/ephemera/oct7-01.htm> (articles).

³² QUACKERY at 23-24.

In the Progressive era, Congress and several states enacted legislation aimed at improving the lot of those whose health, safety or rights were imperiled by commercial practices in unregulated markets. Two federal statutes had particular impact on the patent medicine industry and, thus, influenced the commercial setting for the controversies mirrored in the *Dr. Miles* case. They were the Trademark Act and the Pure Food and Drug Act.

1. The Pure Food and Drug Act of 1906

Public concern about the safety of food processing and patent medicines exploded into countrywide uproar with publication of *The Jungle*, Upton Sinclair's 1906 novel. The story was set in fictionalized "Packingtown" but was taken as an indictment of Chicago's meat packers, an indictment that quickly broadened into condemnation of the entire food processing industry.³³ President Teddy Roosevelt was infuriated over the dismal failure of inspectors in the Department of Agriculture and bullied Congress to act quickly. Sinclair's book together with investigative journalism about the patent medicine industry mobilized public opinion to overcome the well-organized lobbying efforts of the Proprietary Association, the American Newspaper Association, and their food industry allies. After years of dilatory debate, a reluctant Congress swiftly passed the Pure Food and Drug Act before the New Year.³⁴

Unlike the 1938 law that would establish the Food and Drug Administration, the 1906 statute did not regulate ingredients in patent medicines. Nor did it call for government inspection of drug products. Neither alcoholic nor narcotic content was prohibited.³⁵ The statute sought only to remedy what we today would call informational asymmetries – patent medicine's combination of secret ingredients and unsupported therapeutic claims. What the 1906 statute required was accurate labeling of ingredients, and therapeutic claims free of fraudulent and misleading statements. Of the two requirements, the obligation to list ingredients had the greater impact.³⁶

³³ My colleague Ed Purcell reminded me that Sinclair intended to indict the working conditions not the food products and that the response reflected middle class concern with consumer issues rather than sympathy with efforts to help labor.

³⁴ Pure Food and Drug Act of 1906, Pub. L. No. 59-384, 34 Stat. 768, 768-70; for an overview, see <http://www.fda.gov/oc/history/resourceguide/background.html>. The press strenuously opposed the statute. GEORGE SELDES, *FREEDOM OF THE PRESS* (1935); JAMES YOUNG, *PURE FOOD* (1989); TOADSTOOL at Ch. 14; Wallace Janssen, *Outline of the History of U.S. Drug Regulation and Labeling*, 36 *FOOD DRUG COSM. L.J.* 420, 421-422 (1981); OSCAR ANDERSON, *THE HEALTH OF A NATION* 1-16 (1958). In 1848, Congress banned "the Importation of Adulterated and Spurious Drugs and Medicines," 9 Stat. 237. Vincent Kleinfeld, *Legislative History of the Federal Food, Drug, and Cosmetic Act*, 50 *FOOD & DRUG L.J.* 65 at n. 2 (1995).

³⁵ The Smoking Opium Exclusion Act of 1909, 21 U.S.C. §§ 176-185 banned opium imported for smoking purposes. The Harrison Act of 1914, ch. 1, 38 Stat. 785, prohibited distribution of opiates, including morphine and heroin, and cocaine outside medical channels. <http://www.druglibrary.org/schaffer/Library/studies/cu/cu8.html>. FRANKLIN ZIMRING & GORDON HAWKINS, *THE SEARCH FOR RATIONAL DRUG CONTROL* 57 (1992); CAROLINE ACKER, *CREATING THE AMERICAN JUNKIE* 13 (2002).

³⁶ The Department of Agriculture, Division of Chemistry, was charged with enforcing the new law by seizing adulterated or misbranded articles on the market. John Swan, *Food and Drug Administration, in A HISTORICAL GUIDE TO THE U.S. GOVERNMENT* at 248, 250 (George Kurian, ed., 1998).

Congress intended to rein in false or misleading therapeutic claims by prohibiting product misbranding. But a surprising Supreme Court decision would give a narrow reading to the statute's crucial language of "misbranded" that excluded false or misleading statements about the drug's curative effect. Although Congress quickly passed an amendment which expanded the definition, the Agriculture Department continued to lose enforcement actions because courts required proof of fraudulent intent.³⁷ In consequence, the statute had limited deterrence effect on unsupported therapeutic claims.³⁸

The 1906 statute's requirement to list ingredients had greater impact because it turned unwanted light onto the substantial amounts of alcohol and narcotics in patent medicines.³⁹ The new labels informed not only the consuming public but also the Treasury Department, which collected excise taxes. Soon hundreds of patent medicines could be sold only as alcoholic beverages. Some of the most popular curatives, each for their own reasons, quickly lowered alcohol content. PINKHAM'S VEGETABLE COMPOUND did so to retain its reputation as a gentle restorative for women, and remained the leading brand in its large demographic niche. But PERUNA was not so fortunate. As one large distributor lamented, "Peruna is nowhere. We used to get a [train] carload, even two carloads a month. Now we hardly handle a carload in a year." After the new label revealed that it was nothing more than alcohol and flavored water, herbal content was added and alcohol level lowered to avoid the category of alcoholic beverage. Sales of the long-time market leader plummeted, apparently because less alcohol together with herbs having "slight laxative" qualities gave the new potion an unappealing flavor and undesired effect. PERUNA never recovered its popularity.⁴⁰

For the most part, the ingredient labeling requirement weeded small and marginal firms out of the market, in consequence reducing the competition of mavericks and price discounters. Although the market became more concentrated, numerous firms remained and consumers benefited from the new market information. Moreover, a growing number of the larger firms had already begun to produce more "ethical" drugs – that is, they were already disclosing the ingredients in over-the-counter medicines and developing prescription drugs marketed directly to physicians.⁴¹

Passage of the food and drug law seemed to rein in the excesses of trade secrecy and product puffery and, with them, the dangerous extremes of competition in the patent medicine

³⁷ United States v. Johnson, 221 U. S. 488 (1911). The term "misbranded . . . shall apply to . . . any *statement*, design, or device regarding such article, or the ingredients or substances contained therein which shall be false *or* misleading . . ." [emphasis added] The 1912 amendment would require statements to be false *and* misleading. Pub. L. No. 62-301, 37 Stat. 416, 21 U.S.C. § 10; Swan, *supra* note 35.

³⁸ MEDICINE SHOW at 169-70.

³⁹ Under separate authority, the Treasury Department was charged with collecting taxes on alcoholic beverages and, for some periods, on patent medicines. QUACKERY at 99-101, 162-63.

⁴⁰ QUACKERY at 101. TOADSTOOL at 125-30.

⁴¹ *Id.* at 206-07, 248-49. "Ethical" drug manufacturers voluntarily listed their ingredients. Direct marketing to physicians raised its own problems, whether the courting of physicians with financial incentives, their dependency on drug company literature for information or their reliance on recommendations of salesmen in the face of overwhelming amounts of information or inadequate training. Moreover, many medical journals, including the AMA Journal, continued to accept their advertising. *Id.* at 206-210; QUACKERY at 27, 207.

business that threatened health and safety of consumers. The statute did change producer behavior, although questions remained about the degree of benefit when weighing actual improvements in product information and in the products themselves against harm associated with increased market concentration. A second piece of legislation, the new trademark statute, had less obvious but nonetheless significant effect on product information and market concentration.

2. The Trademark Act of 1905⁴²

Large consumer-product firms that developed national distribution networks together with strong brand identities had been lobbying Congress to pass a federal trademark law since the late 1860s. Until Congress passed the Trademark Act of 1881, brand protection rested entirely within the province of state law. On the surface, the legislation seemed to change little because Congress enacted a narrowly written statute that applied only to international commerce. Thus patent medicine marketing and the industry dynamics of product differentiation had to make do, for the most part, with state common law protections. Still, the 1881 statute did provide for federal registration and, with it, a Trademark Office available for settling domestic priority disputes between rival claimants. And there was even a bit more to the story: Because federal judges were still breathing the air of *Swift v. Tyson*, the common law doctrines of trademark and trade-name protection rested comfortably in the interstices of the new federal registration scheme.⁴³

Moreover, national registration saved trademark owners the time and expense of successive state registrations. In this respect, federal registration was particularly valuable to leading patent medicine makers because it gave constructive notice to all would-be competitors that nationwide trademark rights were claimed. In practical effect, federal registration changed the fundamental doctrine of state common law that trademark protection required commercial use in a particular locale. With the national system, registration plus use in any locale was enough for national exclusivity. Once again, the new federal system was particularly valuable to leading firms because registration itself extended their brands into all states and locales.⁴⁴

The 1905 statute altered the landscape of trademark protection in a second significant respect: It effectively lowered the owner's burden of proving trademark infringement. Under the prevailing common law standard, the owner had to prove not only that the registered and accused marks were virtually identical but also that the infringement was intentional. In place of these stringent elements, the new statute merely required the owner to show that buyers were

⁴² Act of Feb. 20, 1905, 33 Stat. 724.

⁴³ See, e.g., L.E. Daniels, *The U.S. Trade-Mark Association*, 33 TRADE MARK REP. 3 (1943); Robert Merges, *One Hundred Years of Solicitude, 1900-2000*, 88 CAL. L. REV. 2187 (2000). PERITZ, COMPETITION POLICY at 29; *Swift v. Tyson*, 41 U.S. (19 Pet.) 1 (1842). Congress was timid because the Supreme Court had struck down its 1879 trademark statute as unconstitutionally founded on the Progress Clause, U.S. CONST., art. I, § 8, cl. 8. *Trade-Mark Cases*, 100 U.S. 82 (1879). Subsequent legislation was enacted under the Commerce Clause, U.S. CONST., art. I, § 8, cl. 3.

⁴⁴ *United Drug Co. v. Theodore Rectanus Co.*, 248 U.S. 90 (1918) (constructive notice). Prior local trademarks remained effective but could not expand into other locales. See generally MERGES ET AL., INTELLECTUAL PROPERTY IN THE NEW TECHNOLOGICAL AGE 628-31 (2004).

likely to confuse the two marks.⁴⁵ At the time, the use of copycat marks was a common practice in the patent medicine industry. The new law would prohibit the practice by allowing trademark owners to enjoin competing marks with less prominent similarities. Both changes – the nationalization of mark effectiveness and the broader notion of mark similarity – provided conditions for increased concentration in the patent medicine industry by strengthening the exclusionary power of established trademarks. But a growing group of mavericks, the discount drug wholesalers and retailers, were raising the temperature of price competition.

II. *Dr. Miles Medical*: “The Cut-Rate Business” Challenges “The Direct Contract Plan”

The litigants were fierce commercial adversaries. While Dr. Miles employed strategies to maintain prices and differentiate its brand in the densely populated market for proprietary medicines, Park & Sons fought to expand its discount wholesaling business. A producer and wholesaler since the 1840s, Park became a leader in the “cut-rate business” that employed the increasingly efficient distribution networks for consumer goods.⁴⁶ At the same time, Miles, in concert with other large patent medicine makers, sought to stem the growth of discounters by adopting standard form contracts to control product distribution and pricing, and by refusing to deal with discounters. The procession of cases seeking to enforce the contracts and their resale price maintenance provision evidence their widespread if not universal adoption, which was orchestrated by the Proprietary Association, which also organized the large manufacturers’ use of standard advertising contracts. Miles and Park were courtroom veterans well-versed in the era’s legal battles over mass distribution and retailing. It was inevitable that their paths would cross and more than coincidence that their rivalry would lead to the Supreme Court.

A. The Doctrinal Framework: Property Rights and Restraints of Trade

The case arose in the early years of the Sherman Act, a time when the relationship between the statute and the preceding common law of trade restraints was still in flux. On the one hand, Supreme Court decisions such as *Trans-Missouri Freight Association* (1897) and *Northern Securities* (1905) had announced that the statute was not to be interpreted as a codification of the common law. On the other, the Supreme Court in *Addyston Pipe* (1899) had approved the approach taken in Judge William Howard Taft’s opinion below, which portrayed common law doctrine as consistent with the Anti-Trust Act. Taft had written his influential opinion for the Sixth Circuit, the site for the two leading patent medicine cases, including *Dr. Miles*, although Taft would not author those opinions. But federal judges, embedded in the common law mind-set of *Swift v. Tyson*, found Taft’s approach attractive because it permitted them to address trade restraint claims in corresponding terms of the statute and the common law. The section places *Dr. Miles* in this jurisprudential context by examining the parties’ participation in prior litigation involving the industry-wide “direct contract plan of marketing

⁴⁵ The statutory burden of proof tracked the state common law action for unfair competition, which was used to good effect by Nabisco, Coca Cola, and other leaders in the emerging national markets for consumer goods. See, e.g., *National Biscuit Co. v. Baker*, 95 F. 135 C.C.N.Y. 1899 (“Iwanta” and “Uneda” biscuits); *Moxie Nerve Food Co. v. Beach*, 33 F. 248 (C.C. Mass. 1888) (“Noxie” and “Moxie”); ALFRED CHANDLER, JR., SCALE AND SCOPE 63-65, 168-70 (1990); MERGES, *supra* note 42, at 2205-10.

⁴⁶ See *Fowle v. Park*, 131 U.S. 88 (1889).

proprietary preparations.”⁴⁷ With that framework set in place, the section turns to the *Dr. Miles* case.

1. Standard form contracts and Dr. Miles

Miles would file suit against Park with a confidence borne of success in three prior cases that upheld the contract plan for maintaining resale prices. The triplets offer valuable insights into both industry practices and the era’s competition policy. In the first case, Miles sued a discounter to enforce the “direct contract plan,” describing itself as a company that

. . . manufactures proprietary medicines . . . under formulas which are secret, and . . . under trade-names, and . . . possesses, as far as it legally may, an exclusive monopoly. The company has adopted an elaborate system to control the prices, at wholesale and retail, of its articles, and insure sales of its articles at uniform prices.⁴⁸

By “exclusive monopoly,” Miles was asserting its trade secrets and trade-names as the ground for immunizing its contract system for setting resale prices from the common law of trade restraints. Its “elaborate system” was portrayed as the contractual exercise of a lawful monopoly embodied in its intellectual property rights. The court agreed and issued a permanent injunction.⁴⁹

In the two subsequent cases, Miles would make the same argument with the same result. The first consolidated three suits against Platt, a retail druggist who discounted not only Miles patent medicines but also those of Hartman’s PERUNA, the largest selling patent medicine, and those produced by members of World’s Dispensary Medical Association, a national trade association. All three plaintiffs sought injunctions to enforce “what is known as the direct contract plan of marketing proprietary preparations.”⁵⁰ They alleged that Platt tortiously “caused complainant’s . . . agents to violate their contracts and supply the goods to him.”⁵¹ Platt asserted the antitrust defense that the plaintiffs “conspired . . . with a number of druggists to . . . fix and maintain an exorbitant [sic] and arbitrary price for all kinds of medicines . . . and [to] restrict . . . competition in the sale thereof, with intent thereby to compel the public to pay a higher price . . .”⁵²

The court rejected Platt’s antitrust defense, citing the common law doctrine that “trade

⁴⁷ *Miles Medical Co. v. Platt*, 142 F. 606, 607 (N.D. Ill. 1906) (“direct contract plan”). *United States v. Trans-Missouri Freight Association*, 166 U.S. 290 (1897); *Northern Securities Co. v. United States*, 193 U.S. 197 (1905); *United States v. Addyston Pipe & Steel Co.*, 85 Fed. 271 (6th Cir. 1898), *aff’d*, 175 U.S. 211 (1899).

⁴⁸ *Miles Medical Co. v. Goldthwaite*, 133 F. 794, 795 (C.C.D. Mass. 1904).

⁴⁹ *Id.* On the dephysicalization of property, see PERITZ, COMPETITION POLICY 69-72; MORTON HORWITZ, THE TRANSFORMATION OF AMERICAN LAW 145-68 (1992); Kenneth Vandavelde, *The New Property of the Nineteenth Century*, 29 BUFF. L. REV. 325 (1980); John Nockelby, *Tortious Interference with Contractual Relations in the Nineteenth Century*, 93 HARV. L. REV. 1510 (1980).

⁵⁰ *Miles Medical Co. v. Platt*, *World’s Dispensary Medical Ass’n v. Same*, *Hartman v. Same*, 142 F. 606 (N.D. Ill. 1906).

⁵¹ *Id.* at 607.

⁵² *Id.* at 608.

secrets . . . owners . . . may sell them on such terms as they please, may withhold them from one person while selling to others, and may fix any price in their sole and exclusive discretion.”⁵³ The underlying policy was protection of “the property right . . . in the secret process. . . . The right of a patentee, owner of a copyright, or owner of a secret process is merely the right of exclusion or debarment.” The resale price maintenance provision was a “lawful and proper” exercise of *property* rights denominated “exclusive monopolies.”⁵⁴ The *contract* question of trade restraints was “collateral.” It was collateral because Miles and the others did “not in any way claim through or under the unlawful combination in this action.”⁵⁵

Thus the court drew on the formal distinction between common law contract and property rights, and thus between restraints of trade and restraints on alienation, although both restrained competition. The court treated Platt’s defense as turning on whether the plaintiffs’ intellectual property rights fell into the recognized category of “exclusive monopoly,” which would permit them to impose downstream restraints on alienation that would run with the goods. No contractual restraints were necessary and so the common law contracts doctrines of trade restraints would not come into play. Argument over the relationship between these two threads of common law competition policy would re-appear in subsequent cases involving the industry-wide contract system.

In the third case, Miles sued Jaynes Drug Company, again seeking an injunction to enforce its contract system.⁵⁶ Here, the court did take up the contract issue of whether the resale price provision should be prohibited as a restraint of trade. The outcome was no different. The court moved without hesitation from the doctrine that IP rights permitted restraints on alienation of property, to the tenet that contract provisions exercising those IP rights were permitted restraints of trade:

Contracts . . . concerning articles made under trade secrets, the same as similar contracts concerning articles made under a patent or a copyright, are outside the rule of restraint of trade, whether at common law or under the federal statute.⁵⁷

The *Jaynes* court was unconcerned that “[t]hese contracts are in force between [Miles] and nearly all the wholesale druggists of the country and over 40,000 retail druggists.” In effect, the decision closed price competition in the industry by permitting Miles and its rivals to rely on “the direct contract plan” to restrain the “knavery” of price discounters.

2. Standard form contracts and John D. Park & Sons

Park, too, was a veteran of the industry’s contract wars. Before its court date with Miles, the discounting wholesaler was party to two major cases that arose from its attempts to sidestep the two complementary standard contracts used in patent medicine markets. In the first, Park

⁵³ *Id.* at 609.

⁵⁴ *Id.* at 610-11.

⁵⁵ *Id.*

⁵⁶ *Miles Medical Co. v. Jaynes Drug Co.*, 149 F. 838 (C.C.D. Mass. 1906).

⁵⁷ *Id.* at 841-42.

sued the National Wholesale Druggists' Association (NWDA) in the New York courts, seeking to enjoin enforcement of the wholesalers' standard contract. In the other, Samuel Hartman sued Park in federal court, asking for an injunction against the discounter's continuing attempts to obtain PERUNA, the industry leader, outside the price-setting provisions in the manufacturers' "system of contracts." Unlike the uniformly narrow view of competition policy expressed in the Dr. Miles cases discussed above, these reflected sharply different positions in the competition policy debate over nationwide standard contracts.

a. The NWDA case

In 1896, Park filed suit against the NWDA, which was "formed by the co-operation of [125] wholesale druggists and manufacturers of proprietary medicines for mutual benefit and protection." Manufacturers, who were non-voting members of the association, refused to do business with Park because he did not abide by the contract's pricing provisions. Rather, Park sought to buy at a discount and then sell to retailers in the "cut-rate business." The New York state court initially issued a preliminary injunction⁵⁸ on the rationale that the contracts likely were restraints of trade but later withdrew it on a property rights rationale:

The sacred right of the toiler to earn the means of subsistence . . . always will be recognized. . . . [I]nventive skill, even though applied to medicinal compounds, may yet have protection from outlawry if the inventor reasonably uses his property rights He may join with others in similar need . . .⁵⁹

After seven years of grinding litigation, the Court of Appeals of New York finally affirmed dismissal of Park's claims. The state's highest court split 4-3 over the imperatives of competition policy and the effect of the standard sales contract on consumers. The majority concluded that the NWDA contract did "not operate against the rights of the general public. . . . because wholesale dealers have not secured the authority to . . . restrict either the price or the quantity sold." The concurring judge, the swing vote in this case, emphasized that the contract "attempts no restraint whatever upon the manufacturer in making prices" and observed that the wholesalers' only interest was uniform prices. The dissenting faction disagreed sharply, calling the majority's view "a plain perversion of the complaint to say that it involve[es] merely the right of a manufacturer to sell his goods to whom he will."⁶⁰

The majority configured the contours of its competition policy by aligning the interests of association members and consumers against those of price discounters. The opinion began by adopting the trial court's view that "inventiveness" justified the manufacturers' control over "goods . . . covered by patent rights and trademarks, which give the proprietors the exclusive right of specifying prices . . . and . . . the right also to require dealers to maintain the prices specified." The majority then characterized consumer interests in terms, surprising to modern readers, of "a uniform price in all sections of the country." And it was patent medicine

⁵⁸ Park & Sons Co. v. NWDA, 50 N.Y.S. 1064 (S.Ct., N.Y.Cnty, 1896) (page numbers not available for lower court opinions in Westlaw system).

⁵⁹ Park, 64 N.Y.S. 276, 277-78 (S.Ct., N.Y. Cnty, N.Y. 1900).

⁶⁰ 175 N.Y. 1, 19, 22, 31 (N.Y. Ct. App. 1903).

manufacturers' exercise of their intellectual property rights that authorized the NWDA as intermediary to satisfy that preference. In the majority's view, "[w]hile public policy demands a healthy competition, it abhors favoritism, secret rebates, and unfair dealing, and commends the conduct of business in such a way as to serve all consumers alike."⁶¹ The danger of unhealthy competition lay in discounters like Park, who

could command large capital, and by reason of this they could purchase proprietary goods in larger quantities and more cheaply than the other wholesale and jobbing druggists. . . . [T]hus they are enabled to undersell and drive out of business the small merchants in their vicinity.⁶²

Apparently, the court dressed all large firms, including discounting wholesalers, in the populist rhetoric of monopoly. It saw them all as villains engaged in the commercial buccaneering associated with the era's "Robber Barons"—Andrew Carnegie in steel, Cornelius Vanderbilt in railroads and, of course, John D. Rockefeller in his Standard Oil Trust.

The opinion reflects a tension in the era's twin rhetorics of monopoly. On the one hand, courts adopted the technical common-law doctrine of legal or exclusive monopoly to permit contracts that exercised intellectual property rights to restrain downstream alienation of goods, although clearly anticompetitive. On the other hand, a populist discourse of monopoly gave voice to widespread concerns about the power of large firms to corrupt politics and to harm both consumers and the small independent firms that were seen as the country's economic and political backbone. The New York court's populist rhetoric did not, however, invite inquiry into whether lower wholesale prices were actually attributable to favoritism and secret rebates or to quantity discounts and other legitimate efficiencies. It was enough that Park was seen as "command[ing] large capital."

In this view, consumers benefited because the NWDA enabled the "little storekeeper" to compete on equal footing with the "great merchants." But this approach did not take account of the market reality that the NWDA contract worked hand-in-glove with the manufacturers' own contract system, which "fix[ed] . . . a selling price by the druggists." Caught in this economic web of restraints, consumers would uniformly pay more than the discount prices Park's druggists wanted to charge. But lowering prices was less important to the court than remedying the unhealthy competition associated with the populist vision of monopoly's political and economic power to corrupt and control. Still, Park was not a large firm like Standard Oil, not even in comparison to manufacturers such as Miles and Hartman. Moreover, political and economic power to control and corrupt could reside in trade associations of small firms as well as the monopolies: Indeed, the NWDA who sold to "little storekeepers" actually "represented 90 per cent. of the wholesale jobbing trade of the United States."⁶³

At bottom, the NWDA, "little storekeepers" and patent medicine manufacturers shared two economic interests. As the concurring opinion put it, they were all concerned, first, about

⁶¹ *Id.* at 9-11. It is unclear whether the court recognized that the patent medicines were not actually patented.

⁶² *Id.*

⁶³ *Id.* at 14, 21. Similar market relations currently spur debate over the impact of WALMART stores.

keeping large-volume discount wholesalers like Park from introducing price competition and, second, about immunizing full-price wholesalers from the pressures of large-volume discount retailers.⁶⁴ In short, they all wanted to protect their profits from price competition. And so, while the NWDA enforced price uniformity, the manufacturers set the price levels. The two standard contracts worked in tandem to restrain price competition and protect not only “little storekeepers” but also branded manufacturers and the network of distributors that linked them.

The New York court majority confined its analysis to the NWDA wholesalers contract directly at issue in the case. In passing, however, it recognized both the manufacturers’ power to set prices and its broader implications:

This plan . . . is not one confined to the sale of proprietary medicines, but is one that has been adopted by many manufacturers of merchandise and other goods where manufacturers have established a trade-mark, and have gained a reputation which they wish to maintain throughout the country . . . They have consequently established prices at which their goods shall be sold to the consumer, and require all wholesale and retail dealers to supply the consumer at the price list established. The decision, therefore, reached herein, may largely affect the plan of conducting business in other articles of commerce.⁶⁵

The broader implication, largely unrecognized in modern accounts of the era, was that the industry standard contract was a widespread method for restraining trade, no less effective than industry consolidation by merger and cartel.

Although the pleadings also confined the New York court’s dissenters to the NWDA wholesale contract, that was enough for them to conclude that

. . . the association was organized . . . for the purpose of monopolizing and controlling the business of wholesale druggists and jobbers in the sale of proprietary articles or patent medicines in the entire United States, [and] to prevent competition therein.⁶⁶

After pointing out the long line of cases that prohibited such restraints of trade, the dissenting faction insisted that the evidence offered no basis for special dispensation from the common law, even if patent medicines were actually patented, because the patent rights were owned not by the wholesalers but the manufacturers.⁶⁷

Although New York’s high court was unanimous in seeing the broad anticompetitive effects of the two standard contracts’ combined impact, the case produced two sharply different views of the commercial logic driving the industry – the majority’s intellectual property logic of manufacturers rightfully exploiting the fruits of their “inventiveness” and, in the process, benefiting citizens, consumers and small business; and the dissenters’ competition logic of

⁶⁴ *Id.* at 15-16.

⁶⁵ *Id.* at 8.

⁶⁶ *Id.* at 31.

⁶⁷ *Id.* at 44.

wholesalers and distributors, in concert with manufacturers, wrongfully restraining trade to the detriment of consumers.

b. The *Hartman* case

In litigation that would directly influence the *Dr. Miles* case, Dr. Samuel Hartman, the leading patent medicine maker, sued Park to stop it from acquiring PERUNA outside the price restraints of the standard sales contract. Park's answer reprised its antitrust challenge to the nationwide system of contracts.

The lower court rejected Park's antitrust challenge and issued a preliminary injunction. But the appeals court accepted the antitrust defense, found the contract system unenforceable, and dissolved the injunction. This case, like the subsequent *Dr. Miles* litigation, passed through the Sixth Circuit. Both opinions were written by Circuit Judge Lurton,⁶⁸ who would write in *Dr. Miles* that "[t]he acts and conduct against which complainant seeks relief are identically the conduct complained of in the Hartman Case, and the opinion in that case may be referred to for a more detailed statement of the case."⁶⁹

Hartman sought to enjoin Park from tortious interference with the system of contracts, alleging that Park obtained

. . . 'Peruna the Great Tonic' . . . from complainant's wholesalers and retailers by . . . dishonest methods and persuading them to break their contracts with him, and [sold] same to retailers operating 'cut rate drug stores' at less than the wholesale prices fixed by him, who in turn sell to consumers at less than the retail prices so fixed.⁷⁰

Park responded that the antitrust laws prohibited Hartman from setting the resale prices of patent medicines that were sold outright. The argument's foundation was the established common law tenet that once ownership of goods passed to the buyer, control over the goods passed with it. This argument was asserted in several cases discussed above but without success because the courts recognized an exception for contracts that exercised intellectual property rights in the goods.⁷¹ In sum, Park's claim was simply that, without an intellectual property exception, the standard contract's resale price provision stood on its own as an illegal restraint of

⁶⁸ *Hartman v. Park & Sons*, 145 F. 358 (C.C.E.D. Ky 1906), *overruled*, 153 Fed. 24 (6th Cir. 1907), *cert. dismissed on petition of counsel*, 212 U.S. 588 (1908). See *Hill Co. v. Gray & Worcester*, 127 N.W. 803, 807 (Mich. 1910) (describing dismissal requested by Hartman's counsel). Lurton was soon appointed to the Supreme Court and promptly recused himself from participating in *Dr. Miles*.

⁶⁹ *Miles*, 164 Fed. 803, 804 (6th Cir. 1908).

⁷⁰ *Id.* at 359.

⁷¹ But the very core of the property-based exception to free trade was controversial. The Supreme Court earlier showed reluctance in permitting restraints to run with patented goods. *Keeler v. Standard Folding-Bed Co.*, 157 U.S. 659 (1895). Moreover, the Court would soon hold that copyright ownership itself did not allow the seller to "qualify the title of a future purchaser." That is, restraints on alienation would not run with copyrighted goods. *Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 351 (1908). Finally, the Court would conclude that notice of restraints affixed to patented goods exceeded the statutory grant of legal monopoly. *Motion Picture Patents Co. v. Universal Film Mfg. Co.*, 243 U.S. 502 (1917). These limits on restraints on alienation are known as the first-sale or exhaustion doctrine and remain part of modern patent and copyright law.

trade.

Park advanced the argument in two stages. First, he asserted that the standard contract was an illegal trade restraint unless a patent or copyright brought the special exception into play; here, PERUNA enjoyed only trade secret protection. Judge Cochran rejected Park's argument: "As applied to things made under a secret process, it lacks this favoring circumstance. But it would be illogical to argue therefrom that so applied it was unlawful."⁷² In short, falling outside the patent and copyright exception made the Hartman contracts open to scrutiny but not unreasonable restraints of trade *per se*.

Park moved to the second stage of argument – that the contract system, even if not categorically illegal, "contravenes the common-law rule invalidating contracts in restraint of trade." For guidance in determining whether the Hartman contracts were unreasonable restraints, the court turned to Judge Taft's opinion for the Sixth Circuit in *Addyston Pipe* (1898), an opinion whose harmonization of common law and Sherman Act doctrines had been approved by the Supreme Court.⁷³ Taft had developed the common-law distinction between direct and ancillary restraints, a distinction that depended on the contract's main purpose. If the main purpose was to restrain trade by, for example, fixing prices, then the restraint was deemed direct and thus *per se* illegal. But if the contractual restraint was ancillary to a lawful purpose, then the court would determine whether the particular restraint was reasonable in the circumstances.

Cochran turned first to prior cases and observed that "the whole trend of authority is favorable to the validity of the system." Then applying Judge Taft's approach, the judge concluded that the resale price provision, like a seller's covenant not to compete in the sale of a business, was "ancillary or collateral to the main purpose of a lawful contract, to wit, a sale of the medicine. . . . The sweeping principle which has taken form in Judge Taft's [analysis] . . . upholds it."⁷⁴ The contract system was a permissible restraint of trade.

Hartman's victory, however, was short-lived. On appeal, Judge Lurton wrote for the Sixth Circuit:

Even if the lower court is right in characterizing the restraint as ancillary to a contract for sale, the restraint is unreasonable. . . . The single covenant might in no way affect the public interest, when a large number might. The plain effect of the 'system of contracts,' is . . . first, to destroy all competition between jobbers or wholesale dealers in selling complainant's preparations. . . . Next, all competition between retailers is destroyed. . . .⁷⁵

Hartman's industry-wide contract system had broad anticompetitive effects that rendered it an unreasonable restraint of trade. Moreover, Lurton rejected the lower court's view that patent

⁷² 145 Fed. at 359-70. *Chadwick v. Covell*, 151 Mass. 190, 191 (1890) (Holmes, J.).

⁷³ 145 Fed. at 387; *Addyston Pipe*, *supra* note 53.

⁷⁴ *Id.* at 381-83. Although *Addyston Pipe* involved what current readers call horizontal restraints, the modern distinction between vertical and horizontal was not yet part of competition policy, whose foundation of classical economics derived from freedom of contract, regardless of the parties' relationship.

⁷⁵ *Hartman*, 153 Fed. 24, 41-42 (6th Cir. 1906).

protection holds no special purchase in the analysis of trade restraints. His approach applied the technical common-law doctrine of “legal monopoly,” which is sharply different from the modern conception of economic monopoly: “So far as the machine was the subject of patent its use was lawfully a monopoly, and therefore no contract relating to it could be condemned as creating a monopoly.”⁷⁶ That is, a patent was a legal monopoly in the technical sense that it granted the holder an immunity from common law prohibition of contracts in restraint of trade. But the dispensation derived from trade secrecy was more limited:

To say that the owner of this secret need not make the medicine, nor sell it when made, unless it suits his convenience, is true. But the same thing may be said of the man who grows potatoes. He need not grow them, and need not sell them when grown. But, if something be conceded in favor of an article which no one can produce except the owner of the formula over one which any one can produce, what shall it be? There is no statute creating a lawful monopoly such as seems to take articles made thereunder without the rule against illegal restraint. . . . None of the reasons which apply to patented articles, copyrighted productions, or to restricted disclosure of the secret formula itself apply to the product of the formula.⁷⁷

Federal legislation granted an immunity from liability for restraints of trade to contracts for the sale of patented and copyrighted goods. But where the goods were protected only by trade secrecy, the dispensation was limited to the secret information. Goods produced by secret formula were treated no differently than potatoes. The court of appeals concluded that Hartman’s system of contracts was an unreasonable restraint of trade.⁷⁸ The opinion explained:

[Hartman’s counsel] averred that the “system” had and will accomplish the suppression of “the competition plan” and “greatly benefit your orator in his business by increasing the sales of and demand for his remedies.”. . . [But] the whole economic system which has made our civilization is founded upon the theory that competition is desirable, and the common-law rules against restraints of trade rest upon that foundation.⁷⁹

Counsel for Hartman petitioned the Supreme Court but subsequently asked for dismissal because the company stopped using the sales contract at issue in the case. It switched to a consignment contract, which the federal courts were already scrutinizing in the *Dr. Miles* litigation. Hartman and others in the patent medicine industry would wait for the federal courts to rule on their new standard consignment contracts.

Why did the patent medicine manufacturers switch to consignment? Miles and the others would adapt the old consignment form, a centuries-old means of retaining a security interest in goods sold on credit, for the new purpose of allowing the manufacturer to retain title in the goods and thereby hold on to property rights that re-defined resale price maintenance as nothing more than setting prices for *its* goods. The consignment form was, they hoped, a stroke of legal

⁷⁶ *Id.* at 40.

⁷⁷ *Id.* at 33.

⁷⁸ *Id.* at 46.

⁷⁹ *Id.* at 44.

ingenuity that would immunize resale price maintenance from the twin common law strands of competition policy: The property doctrine against restraints on alienation would not apply because the retention of ownership meant no goods would be alienated until consumer sales. Moreover, retention of title would avoid the contracts doctrine of trade restraints because the resale price restraint would run with the goods. Finally, ownership in the goods themselves would provide a more stable legal foundation than the shifting boundaries of “legal monopoly” associated with intellectual property rights. It would be the Supreme Court that ultimately decided the success of the consignment strategy.

B. *Dr. Miles Medical v. John D. Park & Sons* in the Lower Courts

In 1908, Dr. Miles Medical filed the fourth in a series of tort actions for malicious interference with its contract plan, this one against John D. Park, the discount drug wholesaler. Park replied by demurrer, which was summarily sustained. Writing for the Sixth Circuit Court of Appeals, Judge Lurton affirmed dismissal. Just as he had in Hartman’s case against Park, Lurton struck down the standard contract system as an unreasonable restraint of trade – even though the new contract was a consignment.⁸⁰ Revision from sale to consignment made no difference because, in the court’s view,

The scheme is one to enhance or maintain prices by eliminating all possibility of competing rates between either jobbers or retailers, and is quite as effectual in its results as if the contract with the jobber was plainly one of sale.⁸¹

By Judge Taft’s lights in *Addyston Pipe*, the consignment was not an ancillary restraint, but a direct one whose main purpose remained price fixing and whose effects were equally anticompetitive. The new contract was unreasonable *per se*.

Perhaps recognizing the likely appeal of the consignment strategy’s property logic to his more formalist brethren on the Supreme Court, Judge Lurton proceeded to evaluate the consignment on its own terms and found that it was ill-scrivened: Miles’ contract had “too many features which seem inconsistent with a mere agency or commission agreement. All the responsibility of an owner seems cast upon the so-called ‘consignee.’” Despite the best lawyerly intentions, the new form remained a sales contract. Still, for the time being, the opinion sent a clear message to Miles as well as Hartman and the other patent medicine producers that consignments, even if properly drafted, would not receive special treatment under the antitrust laws.⁸²

This case must, after all, turn upon whether there is such identity of character between the statutory monopoly of articles made under a valid patent or copyright and articles made according to some private formula as to exempt them from the principles which

⁸⁰ 164 F. 803, 807 (6th Cir. 1908).

⁸¹ *Id.* at 804. Justice Lewis Powell would adopt this rationale in *Continental TV, Inc. v. GTE Sylvania Inc.*, 433 U.S. 36 (1977).

⁸² 164 F. at 804.

apply to contracts which tend to create a monopoly or restrain trade when the subject is an article not made under a patent or copyright or secret formula.⁸³

Were the policies underlying common-law property rights, Judge Lurton asked, close enough to those underlying statutory copyright and patent to treat them as “legal monopolies” and, thus, as special exceptions to the dictates of competition policy? The answer would be No. Lurton had already concluded that the ownership rights retained under consignment contracts did not stand up to such scrutiny. Turning to trade secrecy, he reiterated the view expressed in *Hartman* that trade secrets were no more exceptional than potatoes.⁸⁴ The question was answered: Common-law property rights did not merit special treatment under the antitrust laws.

The opinion affirmed the trial court’s refusal to enjoin Park from purchasing and reselling at discounted prices DR. MILES ‘RESTORATIVE NERVINE’ and other potions. The new system of consignment contracts was a direct restraint of trade that eliminated competition among wholesalers and among retailers and, thus, was a *per se* violation of the antitrust laws. But Miles would carry the question to the Supreme Court.

C. *Dr. Miles* in the Supreme Court

Writing for the Court, Justice Charles Evans Hughes noted Miles’ statement that the contract plan was adopted by “over four hundred jobbers and wholesalers and twenty-five thousand retail dealers in proprietary medicines in the United States.”⁸⁵ Hughes observed that the contract system was “carefully devised . . . to maintain certain prices fixed by it for all the sales of its products, both at wholesale and retail.” “The principal question,” he announced, “was the validity of the restrictive agreements.”⁸⁶ The Court would invalidate the new contract following the approach taken by Judge Lurton in the case below and in the *Hartman* case, but with one crucial difference: The Court would not declare consignments categorically illegal restraints of trade.

Justice Hughes resolved the issue by scrutinizing the document and finding that the language in Miles’ pleadings as well as in the contract betrayed it as a sale rather than a consignment. Miles offered two well-trod grounds for its validity under the common law as well as the Sherman Act. The first was trade secrecy and its claimed equivalence to letters patent as a special exception to the competition policy embodied in restraints of trade doctrine. The Court rejected the analogy, as did Judge Lurton below, on the rationale that patents are exclusionary rights that Congress rewarded special treatment in exchange “for the advantages derived by the public for the exertions of the individual.” Trade secrecy was a lesser right: “The complainant has no statutory grant” because trade secrecy offered no comparable public benefits of encouraging innovation. There was no special property-based exception to the “public interest in maintaining freedom of trade with respect to future sales.” The Court carried forward the

⁸³ *Id.* at 805.

⁸⁴ *Id.*

⁸⁵ 220 U.S. 373, 374-5, 381 (1911).

⁸⁶ *Id.* at 382.

common law policy which favored free competition by limiting the kinds of restraints that run with real property or chattels after sale.⁸⁷ “A general restraint on alienation is ordinarily invalid” because “it is against trade and traffic and bargaining and contracting.” Without the “legal monopoly” of patent and copyright, there was no special property right that trumped competition policy as the default rule for commercial markets.⁸⁸

Miles’ second argument shifted ground from the property doctrine against restraints on alienation to the contract doctrine that the “liberty of the producer [to] make and sell, or not, as he chooses” should be recognized, even if the new standard form was a contract for sale, because it was a reasonable restraint of trade. But citing a string of sources from the English common law to *Addyston Pipe*, Justice Hughes invalidated the resale price restraint because it was not ancillary to “a sale of good will, or of an interest in a business, or of a grant of a right to use a process of manufacture.” Its main purpose was “to prevent competition among those who trade in” the patent medicines. “[T]he restrictions . . . were invalid both at common law and under the act of Congress We think that [Judge Lurton] was right”⁸⁹ because

. . . the public interest is still the first consideration. . . . [T]he restraint . . . must be found reasonable both with respect to the public and to the parties. . . . [T]he public is entitled to whatever advantage may be derived from competition in the subsequent traffic.⁹⁰

But unlike Lurton’s opinion, the Court maintained a considered silence toward the question of whether a valid consignment contract would provide a safe harbor from antitrust liability. Instead, Justice Hughes found provisions in the contract, loopholes, that permitted outright sales to discounters like Park. The implication was that the property right retained in a proper consignment could have shielded the price restraints from antitrust scrutiny.⁹¹

Justice Holmes dissented, opining that the Court majority “greatly exaggerate the importance to the public of competition in the production and distribution of an article . . . as fixing a fair price.” There were other criticisms along the way that led him to characterize Park and his ilk as “knaves [who] cut reasonable prices for some ulterior motive of their own.”⁹² But in both practical and jurisprudential terms, what was most salient was Holmes’ observation that

. . . by a slight change in the form of the contract the plaintiff can accomplish the result in a way that would be beyond successful attack, if it should make the retail dealers also agents in law as well as in name, and retain title until the goods left their hands⁹³

⁸⁷ Cf. Zechariah Chafee, *Equitable Servitudes on Chattels*, 41 HARV. L. REV. 945 (1928).

⁸⁸ *Id.* at 383.

⁸⁹ *Id.*

⁹⁰ *Id.* at 383-84.

⁹¹ *Id.* at 382-83; *id.* at 386 (Holmes). *United States v. General Electric*, 272 U.S. 476 (1926) (validating resale price maintenance in consignment contract).

⁹² *Id.* at 386.

⁹³ *Id.*

Holmes made plain what the majority only implied – that Miles and fellow members of the Proprietary Association could easily close loopholes and strengthen infirmities to draft a proper consignment contract that would allow them to maintain resale prices. Park, it seems, won the battle but lost the war.

In the end, Holmes got it right – although for the wrong reasons. He got it right not because competition was over-rated but because price competition would be restrained as a result of the powerful immunity reserved for consignment contracts. Indeed, the price restraints would be *per se* legal once the manufacturer retained title to the goods. Holmes recognized that the loopholes would be closed before the ink dried on the majority opinion.⁹⁴

Afterword

The consignment form was a stroke of lawyerly brilliance, no less than the invention of the commercial trust form first adopted by Standard Oil, because it allowed Miles in concert with other patent medicine manufacturers to avoid the imperatives of price competition. The property logic of a consignment exception to competition policy would hold until the latter half of the twentieth century, when the Supreme Court would close it, re-open it, and close it emphatically in *GTE Sylvania*, only to suggest later that it was open yet again.⁹⁵ Regardless of its current status, the consignment form sheds light on the property logics that shape antitrust policy.

Indeed, another powerful property logic drives the current antitrust jurisprudence of vertical restraints. It is the logic of trademark ownership. Although asserted unsuccessfully in the *Dr. Miles* era, trademark ownership and the commercial strategy of branding would later influence the Supreme Court to view markets as bifurcated, as working at distinct levels of intra-brand and inter-brand competition. Trademark ownership would draw a bright line across the terrain of competition with the result that manufacturers were increasingly permitted to impose restraints on downstream alienation of their trademarked goods.

In *White Motor* (1963), the Court declared that a small branded manufacturer could impose non-price restraints on its dealers, on intra-brand competition, when it showed that the restraints enhanced competition against General Motors, Chrysler or Ford, when they enhanced inter-brand competition. The implicit economic logic was that White Motor could not compete on price because it could not match the larger firms' economies of scale. Without dealer restraints to enforce its plan to compete on quality against other brands, White Motors would fail.⁹⁶ If the original impulse was a special solicitude toward small firms often attributed to that era, it dissipated long ago.

⁹⁴ The consignment device had unspoken impact on the market: Only firms with financial resources could do business on a consignment, the traditional instrument for securing credit sales. Consignment was attractive to resellers because they paid only after the goods were sold. The prospect of delayed payment and associated costs of financing distributors and retailers raised financial difficulties for small firms seeking entry or expansion in addition to the high advertising costs. They faced entry barriers in the strictest sense insofar as their borrowing costs were typically higher because they carried greater risk of default.

⁹⁵ *GTE Sylvania*, *supra* note 80; *Bus. Electronics Corp. v. Sharp Electronics Corp.*, 484 U.S. 717, 733 (1988); see Peritz, *Genealogy*, at 511-16, 531-37, 550, 562-67.

⁹⁶ *White Motor Co. v. United States*, 372 U.S. 253 (1963).

GTE Sylvania (1977) would adopt Judge Lurton's view that consignments did not provide a special exception to competition policy at the very moment it announced that inter-brand competition was simply more important than intra-brand. In effect, it was an exchange of property logics – trademark ownership for chattel ownership under consignment. For twenty years, the Court declined to extend the trademark logic of brand competition to price restraints. But in the last decade of the century, Court extended the special dispensation for intra-brand restraints to maintenance of maximum resale prices.⁹⁷ And as this chapter is written, the Supreme Court will likely reconsider the issue in *Dr. Miles* – the *per se* illegality of minimum resale price maintenance.⁹⁸

Much has changed since the heyday of patent medicines. Dr. Miles Medical became Miles Laboratories and found commercial success in the mid-twentieth century with its popular over-the-counter remedy ALKA-SELTZER. In the latter part of the century, Miles merged into the corporate confines of Bayer Laboratories. But what has not changed is that one property logic or another has always provided special dispensation from competition policy. Despite current orthodoxy, branding is not a natural barrier across the terrain of competition; nor is inter-brand competition inherently preferable to intra-brand. It is the property logic of trademark ownership that makes it so by portraying a discounter as a free rider or knave rather than a free trader.⁹⁹

A century after antitrust battles over industry standard contracts that manufacturers used to control the prices of RESTORATIVE NERVINE, PERUNA and other patent medicines, at least two things are clear amidst whirlwinds of change. First, the property logic of trademark protection shapes the modern vertical restraints jurisprudence that allows branded manufacturers broad power to restrain competition in consumer product markets. Second, technologies of distribution and marketing are changing dramatically, as they did a century ago. Indeed, some say the Internet changes everything, as others believed of railroads in their time. That remains to be seen: While new technologies promise wider access to markets and more information about them, technological advances and permitted licensing practices have extended manufacturers' capabilities to retain control over their products by what the common law called restraints on alienation and restraints of trade, the twin doctrines that still define competition policy. Moreover, in today's economy, to the extent that brands organize systems of complementary products strategically developed around technological incompatibilities, the property logic of trademarks immunizes a pervasive structure of trade restraints, as did the widespread use of direct marketing contracts a century ago. We close then with an old question: What role should competition play in shaping consumer product markets driven by new technologies and organized by the exclusionary rights of property holders?

⁹⁷ *Khan*, *supra* note 2.

⁹⁸ *See supra* note 2.

⁹⁹ EDWARD CHAMBERLIN, *THE THEORY OF MONOPOLISTIC COMPETITION* (1933) (Appendix on Trade Marks); Peritz, *supra* note 7 (discussing Chamberlin).