

131

THE ARMY INDUSTRIAL COLLEGE
WASHINGTON, D. C.

Course 1930-1931

"PRICE CONTROL"

Lecture by

Captain Fred E. Hagen, Q.M.C.

March 9, 1931.

PRICE CONTROL

by

Captain Fred L. Hagen, C.M.C.,
Army Industrial College,
March 9, 1931.

INTRODUCTORY

It is not my thought this morning to attempt any complete consideration of the complex subject of Price Control. First, because that is manifestly impossible, even granting a speaker's capacity, to do in the time available. Second, a committee of the School is considering this subject and it is not my desire to anticipate their report. There are, of course, many means and measures which will facilitate in time of war speedy and adequate procurement of needed supplies, but, I venture to say, no other single means will so quickly and markedly tend to bring desired results as will a reasonably effective stabilization of the price structure of the Nation. In the brief discussion which I will make I will confine myself to basic principles and avoid so far as may be possible expression of personal opinions which are not susceptible of satisfactory proof.

We all recognize that no plan to mobilize the inanimate resources of the Nation in time of emergency is complete and dependable unless it visualizes and attempts some solution of the complex and puzzling questions involved in Price Control.

No time can be devoted here to a consideration of the economic relation between prices and the demand and supply of commodities of commerce. Demand, supply and price are three economic factors whose interdependence are recognized by every thinking man. In the work-a-day world about us we see these factors constantly in play, and we note how our complex economic structure is affected by changes in one or the other of them.

In time of war the demand factor for items essential to the prosecution of war becomes insistent and tends to become independent of price. Thus, we have then a seller's market instead of, as in normal times, a buyer's market. Hence, the problem of effective governmental control is then in some degree simpler than the like problem in time of peace. Prices in war rise beyond the peace time range because of these facts

Inflation of the currency due to an increase in volume of currency and also due to an increased rapidity of circulation of currency.

Increased consumption caused by enlarged governmental demand and by augmented purchases by the people as money paid out for war supplies passes to the use of those engaged in production.

Reckless buying, both by the Government and by the people, concurrent with business instability.

Higher cost of production due to the substitution of unskilled labor for expert labor, and due also to the fact that the high cost producers must be called upon to contribute to the needed supply.

Decline in the supply of commodities and of raw materials because labor is diverted to the Army and to munition factories.

High freight, insurance, and interest rates, caused by the inescapable implications of war.

Increased taxation demands by the Government as it struggles to meet the financial needs of war.

Profiteering, which in some degree and in some fashion is present in each war period.

Decrease of normal imports due to the uncertainties and vicissitudes of war disturbance of markets and of shipping facilities.

There are two main purposes to be borne in mind as one visualizes a scheme of price control in war. The first purpose is to protect the civilian population, thereby minimizing labor difficulties, maintaining the morale of the people, and assuring their maximum productive efforts. The second purpose is to stabilize markets, thereby ultimately increasing production, industrial development can proceed effectively at any price level provided that level is reasonably steady. Maximum production in a minimum period of time is assurance of a successful prosecution of the war at least cost, and is further assurance of the earliest possible return to normal conditions.

RESULTS OF PRICE CONTROL EFFORTS IN THE UNITED STATES DURING THE WORLD WAR.

During the World War various methods of price control were tried in the United States. These methods may be indicated under four broad general heads

That generally adopted by the War Industries Board and the Price Fixing Committee which consisted in ascertainment, largely through the Federal Trade Commission, of the cost of production and setting, by agreement with producers, a maximum price which included this cost, plus a designated profit.

The bulk line method, used, for example, in the designation of the prices for fuel, which consisted in the ascertainment of a price which would assure needed supply for a given area and a given period. This method which commends itself in many ways, permitted, however, as did also the first method noted, the low cost producers, which in general were also the large producers, to receive an abnormal profit. The excess profit tax was devised to equalize financial returns of producers.

The method, largely followed by the Food Administration, which set the price at a figure which would permit a reasonable margin of profit to the seller. This method took into account varying costs of dealers. Enforcement depended upon the power of public opinion and upon statutory authority to license dealers and to designate rules for their conduct.

The minimum price method which was adopted by Congress, in the case of wheat, to stimulate production.

Congress fixed the price of one article by legislation, i. e., wheat. The price fixed was a minimum price and the object sought was a stimulation of production. There was argument in favor of including other items than wheat, but one now sees that to have increased the financial involvements and to have expanded the administrative machinery to accommodate the inclusion of other commodities would have seriously interfered with governmental efficiency at a time when the Government was assiduously busied in strictly governmental functions as distinguished from quasi-business functions.

Congress gave the President no powers to fix prices except in the case of coal. It did authorize him--an authority which was not invoked--to enter to some extent into the business of buying and selling, in addition to wheat, also flour, meal, beans, and potatoes.

The Lever Act, which is ordinarily referred to as a Price Control Act--so far as it covered food--was intended to free the channels of trade, so that commodities would move directly and speedily from producer to consumer. It provided

penalties for hoarding, for destruction, and for waste. It did set a penalty for the sale of an article at an unfair price. This feature of the bill was relatively unimportant, was invoked in but few instances, and has been declared to be unconstitutional.

Significant and, in the main, successful efforts, in the field of import and export trade, to control prices and direct supplies, particularly raw materials, to determined uses and to secure needed items of foreign production in exchange for items of home production, were involved in the activities of the Federal Trade Board of the Shipping Board.

Attention should also be given to the activities of the Wool Administration. The method here employed was the accumulation by the Government of the country's entire supply of raw wool and its diversion to uses which would best serve the Nation's war needs.

The efforts of the War Industries Board in the realm of price fixing were directed solely to the securing of a reasonable price for the Government, it being generally recognized that as the predominant purchaser the Government should concern itself in the public interest in the prices it paid. The only concern the War Industries Board gave to prices in the general market was insofar as they affected prices which the Government would have to pay for its own uses.

The Food Administration had no authority to fix prices and made no attempt to do so. It worked through the highly stimulated force of public opinion. It enlisted every housewife as a member of its administrative staff. In every community and state volunteer workers were busy as its agents. It maintained a comprehensive scheme of securing cost and price data. It published daily for particular markets and for particular districts lists of fair and reasonable prices. These determinations were put out as guides merely. The regulatory methods of enforcing fair and reasonable prices with respect to food were two-fold first, the force of public opinion, and second, the licensing power of the Food Administration which enabled it to impose conditions which must be met by the licensees who wished to do business in any particular line. The Food Administration had certain axiomatic principles which must guide us in any plans which we make for any future price control. Mr Hoover indicated that the standard of reasonableness should be determined as the profit which the dealer customarily enjoyed on the same commodity in the pre-war period on an even market under freely competitive conditions, and that the reasonable margin of

profit must be figured upon a cost basis, the fixing of maximum margins of profit, and the disregard of replacement value in fixing margins. The object of the licensing system, he indicated, to be to limit the price charged by every licensee to a reasonable amount over expenses, to forbid the acquisition of speculative profits from a rising market, to keep all food commodities moving in a direct line and with as little delay as practicable to the consumer, and to limit, so far as possible, contracts for future delivery and dealings in future contracts

There has been so much confusion of thought as to what were the gains and failures of price control efforts in the United States during this period--there being on the one hand extravagant assertions as to the efficacy of methods and as to results attained, and on the other hand, extravagant assertions to the effect that, as a practical matter, no measureable influence upon prices was properly attributable to the work of the several Federal agencies--that it is pertinent to attempt to determine just where truth lies

Some beneficial results, direct or indirect, which may be fairly attributed to price control efforts in this period in this country may be here summarized

Stabilization of the industrial and economic life of the Nation, which made possible the incredible war effort put forth.

Stimulation of increased production of needed foods and other raw materials.

Economy in the use of supplies because of the wide publicity given by the Government with respect to its needs and to the needs of the Allies, and because of the emphasis laid on the direct and tangible relation between conservation and victory.

Discouragement of hoarding for the purpose of increasing prices--accomplished through the force of public opinion and through Governmental action

Curtailment in the use of raw materials and of labor energies in the production of nonessentials--accomplished through a variety of indirect methods.

Failures, and admittedly there were failures, may be attributed, not so much to methods and principles and manner of administration, as to the fact that there was a general hesitancy

127

to face the problem as a whole and to meet the issue in one comprehensive, all-inclusive program. There was also an ever-present fear that each new power granted might lodge itself permanently in our administrative structure. Further, in noting causes of failure, record must be made of the incredible contribution of the United States to the needs of the Allies while at the same time its own purchasing activities in its own markets sought to satisfy the voracious appetite of war. To this latter fact alone we may largely attribute the fact that the Civil War and World War price curves are nearly parallel, with no price control efforts in the first period and with many price control agencies in the latter period.

LEGAL ASPECTS OF PRICE CONTROL

The story of attempts to control prices is as old as the story of organized government. No individual or group of individuals who have seized, or who have been charged with, conduct of government have operated long without making some effort to control or fix prices. In the United States the activities of state governments have been more conspicuous and more consistent than have those of the National Government and in consequence the legal power of state governments in this respect have been more definitely determined. With our present economic and industrial structure, it is to be expected that the National Government will take a more and more significant part in efforts directed to the control of the essentials of human life. Because there seems to be so much uncertainty as to the legal powers of the Federal Government with respect to price control, certain principles and rules which apparently have been definitely determined may be indicated.

The Constitution of the United States, in almost the identical wording of the ancient laws of Rome, stipulates that private property shall not be taken for public use except after due process of law and with just compensation.

"Due process of law" has been uniformly interpreted in all civilized governments as referring to judicial determination, rather than legislative or administrative determination.

"Just compensation" is that price which the courts, after investigation and judicial hearing ascertain to be a fair and reasonable reimbursement.

The taking of private property for public use and the use made of it are political functions exercised normally under our form of government by the legislative branch

136

Price fixing, if it operates upon property already owned, which the owner is compelled by governmental authority to sell at a loss, is the taking of private property for public use.

Congress may exercise its constitutional powers with reference to the taking or control of private property, or the fixing or control of prices directly, or through executive agencies

The War Industries Board--either as a creature of the Council of National Defense, or as an arm of the President --had no power to fix price.

An agreement forced by Governmental agencies upon individuals is not a voluntary agreement

The penalty clause of Section 4 of the Lever Act is unconstitutional, because it did not set up an ascertainable offense and an ascertainable degree of guilt, but left to a jury the determination of whether an offense had been committed and what that offense had been, as well as leaving to it its normal functions of determining definite facts.

If Congress authorized a price fixing agency (as it did in the case of coal--the only authority it did give for fixing prices) and a coal dealer sells at a subsequently fixed price and at a loss, he cannot later call upon the Government for reimbursement. His remedy was to refuse to sell, thus compelling the Government to commandeer his property and to proceed upon definitely determined lines

A continuing transaction cannot be affected by price fixing promulgated after the initial steps of the transaction have been taken

Any penalty clause will be construed against the Government if it is vague or indefinite.

In all organized governments the right to take or use private property in emergency for public use, irrespective of legislative sanction when there is not time for appeal to the legislature for sanction, is recognized. Every public officer or citizen who exercises this right on behalf of the United States must understand that he may be later called to account in the courts and here required to

justify the necessity for his act and defend himself against any charge that he proceeded in an arbitrary, or capricious, or malicious manner.

THE PRACTICAL ASPECT OF PRICE CONTROL

The legal aspect of price control is by no means as important as its practical aspect. It is more important to determine whether a government, given even the most arbitrary power, can successfully fix prices and how. So far as known no government has ever failed to attempt some control of prices. Every conceivable device and expedient have been tried and tried again. The story of price control efforts is accessible to every one interested and he who runs may read. Failure and disappointment--almost without exception--are the last words in each recorded story.

Efforts made in China as early as 1122 B.C. are of most interest to the student of price control, because these efforts are the only known efforts that were followed with conspicuous success. For hundreds of years, and until political corruption infested administration, the Chinese Government attempted to balance supply and demand and to keep prices within reasonable bounds. The Chinese political theory took into account, as most price-fixing theories have not, that there are two sets of interests to be considered--those of the producers and those of the consumers. They recognized the whole price question as a symptom and not as the disease itself. They saw that nothing more markedly at once affects the interests of both sides than prices and that price control is, therefore, the great problem for society as a whole. They conceived it to be the task of the superior man to adjust demand and supply so as to keep prices on a level in order to guarantee the cost of the producer and satisfy the wants of the consumer.

The scheme worked out by them with respect to farm products is particularly interesting. In the good crop years the Government purchased a proportion of the surplus crops, thus maintaining the market price. In the poor crop years the Government sold, from its accumulated stores, to the consumers at the market price, thus preventing both speculation and famine. They believed that even if the Government lost money in its transactions, as a matter of fact it did not, the social benefit was greater than the public expense.

A quotation from "The Economic Principles of Confucius and his School," by Huan-Chang Chen, page 447 is of interest

"Prices are controlled by the government. All goods have a fixed price, and its difference is simply according

176

to the quantity. In this way the buyers are encouraged to come in. There is the Master of Merchants in every twenty shops, to fix the price according to the cost. When there is any natural calamity, the merchants are not allowed to raise their price . . . by the raising and lowering of price, the government controls the supply. When a thing is not in existence, the government causes it to exist, when a thing is useful, it causes it to be abundant, when a thing is harmful, it causes it to be extinguished, when a thing is luxurious, it causes it to be lessened There is the government bank to buy the goods which the people cannot sell, and to lend them out when the people need them. In this way the government adjusts the demand and supply, and prices are kept at a fixed level "

The French revolutionary governments, following the overthrow of the Bourbons, tried practically every known expedient to control prices, and with unvarying failure. At least Barbaroux set forth the idea that success could come only in some scheme that would enlist the aid and interest of both producer and consumer. His theory never was reduced to practice by the revolutionary governments.

The most conspicuous effort to fix all prices, including raw materials, finished products, and all manner of services was that attempted by the Emperor Diocletian in Rome, about 350 A.D. Maximum prices were set for every commodity and for every service, and anyone who exacted a higher price was subject to a penalty of death. The historians tell us that the net result was failure and the law had to be repealed because of its impotence in correcting the condition of affairs. There was a general dearth of all the essentials of human life, people no longer brought provisions to markets since they could not get a reasonable price for them. Sixty years after the efforts of Diocletian, the Emperor Julian repeated the attempt in Antioch and with like results. Notice is given to these two instances of price control because we are often assured that a government can succeed if it controls wages as well as prices of commodities.

Students of contemporary history are familiar with the various efforts of the Soviet Government to control prices and supply, and of like efforts of the present Government of Italy. In both of these nations in the period in question the authority and power of the Central Government have been unchallenged and in consequence it would be expected that if success could ever come to price control efforts it could be here reasonably expected. The facts are that in neither instance has the Government apparently been able to do all that which it set out to do.

H I

Three quotations are here presented to indicate opinions as to the practical aspect of Price Control

"The history of government limitation of price seems to teach one clear lesson, that in attempting to ease the burdens of the people in a time of high prices by artificially setting a limit to them, the people are not relieved but only exchange one set of ills for another which is greater. Among these ills are (1) the withholding of goods from the market, (2) the dividing of the community into two hostile camps, one only of which considers that the government acts in its interest, (3) the practical difficulties of enforcing such limitation in prices which in the very nature of the case requires the cooperation of both producer and consumer to make it effective." Miss Mary G. Lacy, Scientific Monthly, June, 1923.

"The experience with price regulation during the war has shown that prices can be controlled without giving rise to a great deal of evasion and without too much running counter to the competitive spirit which animates our industrial society when a great emergency like the recent war fires public imagination and inclines public opinion to favor any measures which are likely to advance the national cause. The best methods of control, however, are those which enlist the cooperation of the people whose interests are to be affected by price regulating measures." Doctor Simon Litman, "Prices and Price Control in Great Britain and the United States During the World War."

"Whereas, it hath been found by Experience that Limitations upon the Prices of Commodities are not only ineffectual for the Purposes proposed, but likewise productive of very evil Consequences to the great Detriment of the public Service and greivous Oppression of Individuals,

Resolved, That it be recommended to the several States to repeal or suspend all Laws or Resolutions within the said States respectively limiting, regulating, or restraining the Price of any Article, Manufacture or Commodity." Journals of the Continental Congress, Vol. XI, June 4, 1778, page 569.

CONCLUSION

No plans for industrial preparedness are adequate unless they take into account the question of control of essential commodities. The control of essential commodities involves the question of control of prices. While there are certain legal

difficulties and certain legal doubts, the situation has been sufficiently cleared to indicate that, moving along certain lines and taking into account certain limitations, Congress has an unquestioned power to exercise control of prices either directly or through the executive branch of government. The important consideration, however, would seem to be not so much what power Congress or the President may have with respect to price control, but what methods can be employed successfully. Assuming as the purposes of price control, the assurance of an adequate supply of all commodities and services needed by the Government in time of war, the stimulation and maintenance of a high and spirited morale in the civilian population, the conservation of the uninterrupted efficiency of the workers so that they may produce what may be needed for the war effort and for civilian consumption--the best methods to be employed are those which take into account both producers and consumers and depend for their enforcement upon voluntary support rather than upon governmental power. In this light, then, some policy similar to that of the Food Administration operating in the whole field and freed of any inadequacies and ineffective features, which as experience has pointed out, would seem to be a profitable field for future study. Fortunately, success in price control efforts is more easily attainable in time of war than in time of peace.

The National Defense Act places upon the Assistant Secretary of War the sole and undivided statutory responsibility of formulating, in time of peace, comprehensive plans adequate to the mobilization--promptly, smoothly and effectively--of those economic and industrial resources of the Nation which are essential to the effective prosecution of war. In the spirit of this legislative mandate, the Assistant Secretary of War and the several Supply Chiefs of the Army, who, in the matter of procurement, are subject to his jurisdiction, have proceeded in the years following the World War in the task of formulating programs for war-time procurement. Their work has involved a detailed study of the economic and industrial resources of the United States. Intensive research has been prosecuted also in the fields of those essential finished articles or raw materials whose supply, either wholly or in part, must come from outside our own borders. The facilities and possibilities of the individual industrial establishments of the country have been studied in cooperation with their respective heads. Data is now at hand, and is continuously revised, showing normal output, and estimates have been made as to potential output under pressure. Requirements of war supplies have been estimated in terms of quantity and type and composition, and to the various industrial establishments tentative assignments have been made of the quantities which it is thought they severally can furnish. Thus, in

some degree, at least, the War Department finds itself today with some comprehensive and dependable information, which will be available upon the outbreak of war, with respect to these questions. What will be needed? When will it be needed? Where can it be procured?

Not the least of the problems which must be stated and solution sought as this war-time program is formulated is the problem of the relation of price and price-control agencies to the satisfaction of these needs. Much study has been devoted to the extensive records of the price-fixing agencies in the World War. Permanent record has been made of the latter deliberate conclusions of the men then devoted to the solution of the problem. Experiences of other like periods and of other nations have been studied. While no fixed and rigid scheme can be set in advance, yet it is felt that in the event of another emergency preliminary ground-work will have been covered. In general, the prime problem of the War Department is to assure the satisfaction of its procurement program speedily and effectively at a minimum cost to the taxpayers. Rational and careful buying in the opening months of another war, based upon dependable knowledge as to requirements, will in large measure eliminate the confusion and turmoil in the business world which insistently demand immediate price control. A steadying influence will also be contributed by the accumulation in peacetime of reasonable reserves of critical items of supply needed in the early stages of war and of such nature that their accumulation after war begins would necessarily involve delay and uncertainty. The need for some later provision for price control is, however, visualized as accompanying any major war disturbance. Congress places upon the Secretary of War the responsibility of satisfying the needs of the War Department in peace and in war in such fashion and manner that the financial demands upon the taxpayers will be kept at minimum strain. It is with respect to this duty that the War Department can now prepare itself for emergency. Inasmuch as it must be prepared to determine fair and reasonable prices which it can pay, data gathered in time of peace will assure efficiency. To the several Supply Chiefs the Assistant Secretary of War, in harmony with statutory authority, has assigned for procurement specific finished articles and specific raw materials for which they will be severally held accountable. Therefore, now, as these Chiefs are preparing their programs of procurement, they are also keeping in mind the responsibility of assuring themselves that prices they will be called upon to pay shall be fair and reasonable.

Thus the Supply branches will be immediately able to go into the market, having in hand a shopping list made up carefully and deliberately. They will go with assurance because they

will have dependable information with respect to sources of supply. They will purchase economically--in the interests of the taxpayer--because they will know what prices are fair and reasonable. They will not upset and confuse business by competition among themselves because to each will have been assigned all of the purchasing of any particular item.

As we visualize the activities of the early months of some future war, we are justified in the confidence that there will not be immediate occasion for Governmental interference with the normal relations of supply and demand and price. Later, as need arises, and one may assume it will arise, the Government can intelligently and deliberately direct its attention to such control of prices as may facilitate the satisfaction of its needs and as may assure the well-being of the people. When that time comes, study now and intelligent procurement theretofore will simplify the legislative solution of a problem which otherwise would be sought in uncertainty and doubt, and accomplished in pain and travail.

Finally it may be stated that so far as the Army and Navy are concerned Price Control is necessary to assure economical procurement, to facilitate a steady flow of materials to Government contractors and to make possible intelligent distribution of war orders. These ends may be secured through a cordial cooperation between the Army and Navy--the predominant purchasers in war of essential items both raw and fabricated, through elimination of competitive buying between these two Government agencies, and through elimination of needless and reckless buying of war materials by them.

The Army specifically may contribute to these results through

- a. A coordination of Army procurement
- b. Elimination of competition between procuring Branches.
- c. Specific control by The Assistant Secretary of War of the procurement of raw materials and services which are constituents of items assigned to particular Branches.
- d. Preparation in time of peace of estimates of probable requirements in war--thus eliminating a reckless and undue strain on the Nation's markets.

MS

- e. The determination, as the war program advances, by specified Branches, under the supervision of The Assistant Secretary of War of a maximum fair price which may be offered for a given commodity, such determinations to be effective for short periods of time and for particular buying areas and to be constantly revised.
- f. The organization in the Office of The Assistant Secretary of War, and in the office of Supply Branches of agencies to consider and determine price questions
- g. The organization in the Office of The Assistant Secretary of War, and in the offices of Supply Branches of Claims and Adjustment Boards which will
 - (1) Eliminate hazards of war contracting, caused by uncertainties as to final settlement.
 - (2) Make final settlement, so far as it may be made administratively, while facts are fresh and data and personnel are accessible.
 - (3) Assure to contractors fair and just treatment

FEH/MS