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Integration and Competition in the Petroleum Industry, by Melvin G. deChazeau, and Alfred E. Kahn

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BOOK REVIEWS

INTEGRATION AND COMPETITION IN THE PETROLEUM INDUSTRY. Petroleum Monograph Series, 3. By Melvin G. deChazeau and Alfred E. Kahn. New Haven: Yale University Press. 1959. Pp. xviii, 598. \$7.50.

This volume is the third and final monograph of a series financed under a grant made to the Yale University Press by the influential American Petroleum Institute. The stipulated purpose of the grant was so that "wholly objective and searching studies be made of the petroleum industry." An editorial board made up of distinguished representatives from the petroleum industry and from the academic world selected the authors to write the studies.¹

The first volume in the series, written by Ralph Cassady, concentrated on price making in the industry—with particular emphasis on the pricing of refined products at the various marketing levels.² Cassady's book was criticized on the ground that while it described in great detail the price mechanisms in the industry, it virtually ignored the controls over production—the "most significant fact in determining the domestic price structure."³

The second monograph by Erich Zimmerman dealt with conservation and the production level of the industry.⁴ This book was said to be more solid and closer to the issues than Cassady's book but was criticized on the ground it lacked in "rigor when engaged in analysis and in compression when engaged in description."⁵

In 1958, deChazeau, co-author of the volume under review, wrote one of the petroleum critiques appendix to *Antitrust Policies*, Simon H. Whitney's two volume study of the effect of antitrust policies on selected industries.⁶ The substance of Professor deChazeau's rather severe criti-

1. The details of the grant are explained in a "Note" following the Preface. Members of the Editorial Board were: Ray B. Westerfield, Chairman, Yale University; John Boatwright, Standard Oil of Indiana; Neil Jacoby, University of California; A. D. H. Kaplan, Brookings Institution; H. H. Marshall, Signal Oil and Gas Co.; and I. L. Sharfman, University of Michigan.

2. RALPH CASSADY, JR., PRICE MAKING AND PRICE BEHAVIOR IN THE PETROLEUM INDUSTRY, Petroleum Monograph Series, 1 (1954).

3. Stocking, Book Review, 44 AM. ECON. REV. 691, 694-95 (1954).

4. ZIMMERMAN, CONSERVATION IN THE PRODUCTION OF PETROLEUM, Petroleum Monograph Series, 2 (1957).

5. Bain, Book Review, 48 AM. ECON. REV. 1066 (1958).

6. WHITNEY, ANTITRUST POLICIES (1958).

cism of Whitney's handling of the petroleum industry is contained in the following two quotations taken from the critique:

If the analyst would contribute either to the understanding of public issues or to their ultimate solution, must he not forsake the broad highway of established historical precedent and struggle through the more rugged and less certain terrain of alternatives that a different public policy or a contrary business decision would have permitted?

In a field as prickly with moot questions and conflicting evidence as vertical integration and competition in petroleum, it is doubtful if any comprehensive treatment of chapter length could be expected to shed much light or convey much conviction on the issues involved⁷

In *Integration* deChazeau and Kahn do in fact embark on the task of exploring alternatives but have they also succeeded in reaching the standards set by deChazeau in his critique?

As to matters of form *Integration* is a thoroughly documented attractively bound volume containing 667 pages of text, plus a sizable bibliography and a detailed index. Included in the text material are twenty-eight useful tables; and, there is a helpful summary at the end of each chapter. The twenty-one chapters in the study are grouped under four major headings.⁸ Part I introduces the issues and contains the usual descriptive background material. The authors pose several basic questions of "public concern."

Is the industry's form of organization in some sense essential to the expanding supply of liquid fuels on which our future may hinge?⁹

Is the massive integration of the industry's dominant firms . . . compatible with socially acceptable competitive objectives?¹⁰

How far and on what conditions should the United States rely on foreign sources of oil?¹¹

7. 2 WHITNEY, *op. cit. supra* note 6, at 454, 456.

8. The headings are: Part I Introduction: The Structure of the Oil Industry and the Problems It Raises; Part II Crude Oil, Integration and Public Policy; Part III Investment and Innovation; and Part IV Integration and Competition in Product Markets.

9. DECHAZEAU AND KAHN, *INTEGRATION AND COMPETITION IN THE PETROLEUM INDUSTRY* 5 (1959) [hereinafter cited as DECHAZEAU AND KAHN].

10. *Id.* at 7.

11. *Id.* at 9. The authors point out two pages later that this issue must remain on the "periphery" of this study.

The complexities of the issues to be discussed are succinctly summarized at the end of the introductory chapter.

The United States petroleum industry is composed of tens of thousands of separate businesses, covering an enormous range in size, influence, and breath of operations. Its behavior is governed not merely by the profit-seeking activities of these private parties, but also in vital ways by a network of government controls, direct and indirect, state and national—regulating output, providing differential tax treatment . . . fixing prices, . . . persuading, threatening, cajoling managers. . . . This aggregation of separate business entities, thus organized and controlled, is expected to safeguard the national defense, conserve scarce resources, reduce prices, improve quality, expand capacity, and protect the competitive status of thousands of private parties whose interests are often flatly opposed.¹²

The next two chapters are devoted to the structure of the industry and to some theoretical and factual ramifications of integration. It is asserted that while the industry “certainly cannot be regarded as monopoly” it just as certainly is “dominated by a relatively small number of companies.”¹³ Although the authors argue that the available facts do not justify Cookenboo’s conclusion that the Standard Companies tend to compete “less independently” against one another,¹⁴ they state:

Size and fewness of sellers inevitably breed recognition of the fact that each can seriously injure and be injured by the others; and this recognition *may* produce policies objectively indistinguishable from conspiratorial joint action.¹⁵

The “rule of capture” explains a “very great deal of the organization and behavior of the industry.”¹⁶ But many other factors are also important.

Each extension of company facilities and specialized managerial interests broadens the scope of exposure to still further

12. *Id.* at 10.

13. This is essentially the same conclusion reached by JOHN H. MCLEAN AND ROBERT W. HAIGH in *GROWTH OF INTEGRATED OIL COMPANIES* (Boston: Graduate School of Business Administration, Harvard University, 1954).

14. COOKENBOO, *CRUDE OIL PIPE LINES AND COMPETITION IN THE OIL INDUSTRY* 74 (1955).

15. DECHAZEAU AND KAHN 28-29.

16. This is the legal principle that oil drawn from subterranean pools belongs to the first surface owner to reduce it to possession even though it may have migrated from under another owner’s land.

opportunities for profitable investment. . . . The die is more likely to be cast for retention of integration and correction of emergent imbalances by further integration rather than by lopping off awkwardly protuberant parts, where the dominant portion of established costs seems to be sunk and the cost of additions is estimated on an incremental basis. Common costs may make it appear uneconomic to slough off functions that, standing on their own financial feet, could not support their own required investment.¹⁷

In addition to conferring many "strategic" advantages integration tends to force competitors to integrate as well. But is massive vertical integration usually in the public interest as some have claimed? While conceding that horizontal monopoly is the "major threat" to a freely competitive economy the authors argue that the defenders of vertical integration minimize "unrealistically the threat that vertical integration, when combined with seriously imperfect competition in some segments of an industry, may itself pose for horizontal competition."¹⁸ The authors suggest that vertical integration in such imperfect markets is likely to reduce the possibility of countervailing power on the opposite side of the market, and to make the industry more "impervious" to new entry. If the integrated form enjoys substantial monopoly power in some of its markets, it may be in a position to apply a squeeze on its competitors at all levels.¹⁹

The principal factors in the economic setting of the industry relate to conditions of supply.

In the absence of regulation, public or private, the vagaries of exploratory success, the law of capture, and the heavy fixed and joint costs at the several stages of production all make the supply of oil and its products unresponsive to price in the short run. A fluctuating and inelastic supply, in the face of consumer demand unaffected by price, constitutes a truly explosive economic force, which, were it not for the long-run surge of petroleum consumption and the steadying hand of the conservation authority on the volume of oil drawn from the earth, could shake the industry to its foundations, and has done so from time to time in the past.²⁰

17. DECHAZEAU AND KAHN 43.

18. *Id.* at 46.

19. *Id.* at 47.

20. *Id.* at 73.

It is in the "quest for stability" in a "potentially explosive" industry that we can begin to find an explanation for integration. The stability sought is that which arises out of "concentrating risks" on a "mutually reinforcing basis."²¹

It can be observed from the sampling of the text presented thus far that *Integration* stresses an analytical rather than a descriptive approach to the industry. Each industry facet is carefully weighed and sorted. Not infrequently the authors confess that no clear cut answer is possible.²²

It is in Part II that the framework is laid for the principle policy recommendations made in the study. Reiterating the argument that vertical integration in imperfect markets creates many difficult issues of public policy, the authors state:

A more obvious instance of an inherently imperfect market would be hard to find in any industry than that provided by the production of crude oil. Abroad, it is controlled by a few giant international firms; at home, it is regulated by state authority. Thus the production, control, and pricing of crude oil become the crux of the perplexing issues posed by vertical integration in petroleum.²³

This last sentence states the central theme of this study. While conceding that prorationing has reduced some wastes and protected the correlative rights of small owners to some extent, the authors argue that:

In the existing mélange of uncoordinated public controls over oil, only the large integrated firm, as buyer and seller of crude oil in many jurisdictions—and particularly the few who control the bulk of world reserves . . . seem to . . . retain enough room for maneuver to protect its own interests.²⁴

Success in oil exploration is no longer mirrored clearly in the market. This is the nub of the matter; prorationing is now able to keep a larger proportion of potential supplies underground.²⁵

21. At this point the authors expressly disagreed with McLEAN AND HAIGH, *op. cit. supra*, note 13, on the basis that the latter explained integration in terms of the pressure of crude supply and the "ebb and flow" of profit opportunities at the various levels of the industry. Later, however, the authors state the main factor influencing integration was the protection it offers against the "uncertainties and instabilities of reliance on imperfect markets." This seems very similar to an argument made by McLean and Haigh.

22. For example, it is stated that no definite conclusions can be drawn as to presence or absence of workable competition for the industry as a whole. DECHAZEAU AND KAHN 55

23. *Id.* at 122.

24. *Id.* at 125.

25. *Id.* at 155.

And though the Texas commission has often denied any concern for price, it is clear beyond cavil that its exercise of control over supplies has had a major impact in snubbing crude-oil price declines.²⁶

The analysis turns to crude oil exploration. Is integration essential if we are to have an adequate supply located in future years? The major companies actually concentrate on developmental drilling rather than on wildcatting. This is reflected in statistics which show that major companies averaged 79% wet on all domestic wells drilled in 1957.²⁷ This coupled with favorable prospects for "lower than average-priced reserves" found off-shore lead to the conclusion that—

Despite rising capital costs of new exploration and development, current trends would not seem to preclude effective performance by independents, acting alone or in cooperative undertakings.²⁸

And why have crude prices had such a strong upward bias coupled with so little downward flexibility since 1936? The main factors are; prorationing; major owned pipelines, price posting practices, and inter-commodity exchanges.²⁹ The interest of the majors in high stable crude prices arises mainly out of their greater self-sufficiency in crude ownership. Under simplified assumptions a crude oil self-sufficiency of 77% would be necessary in order for a fully integrated company to break even if there was a price increase in crude and no increase at all in product prices.³⁰ But if even 50% of the crude price increase can be passed on, only a 38% self-sufficiency ratio is needed to break even. The majors average about 50% self-sufficiency; and, in general, crude price increases have resulted in higher product prices.³¹

In a subsequent chapter the authors quote a part of a 1940 *Fortune* magazine article which gives added weight to the foregoing argument.

26. *Id.* at 163-64. The authors concede that no data exist by which these assertions can be proved "quantitatively or systematically."

27. It is interesting to contrast these figures with the statement frequently made in industry publications and speeches to the effect that eight out of every nine wells drilled are dry holes.

28. DECHAZEAU AND KAHN 182. Another example of curious industry statistics is to be found in the assertions that the off-shore oil has "cost" \$14 per barrel to produce. This figure is derived simply by dividing total exploratory and drilling outlays thus far by the number of barrels that have been actually brought to the surface. Only a tiny fraction of the huge reserves discovered have been allowed above the ground. See the discussion at 160.

29. *Id.* at 183.

30. *Id.* at 222.

31. See *id.* Table XII at 224.

It is . . . clearly in the interest of large integrated companies to keep profits locked securely in the crude oil . . . far away from the point where the refined products meet the pressure of the market. Under such a system gasoline price wars, touched off by dealers, are incessant; but the marketing companies usually cushion the shock before it gets to the crude margin. The general strategy of running an oil company might be defined thus: make big profits on the crude; protect the profits by owning pipelines and tankers so that transportation earnings do not get siphoned off to others; and, finally, own sufficient refining and marketing equipment to dispose of your products at cost or better.³²

Granting that prorationing and the other factors mentioned explain why the majors usually favor high, inflexible crude prices, how are higher crude prices effectuated? In order to answer this question the circumstances surrounding the crude oil price increases in past years were carefully analyzed. In 1953, for example, the price of crude was increased even though economic conditions apparently offered little justification for this action.³³ The authors conclude:

It [the increase] was initiated by a private policy determination and maintained by a combination of private and public actions related only indirectly to cost considerations.³⁴

Turning to world markets it is observed that in recent years an increasing number of independents have been able to acquire interests in foreign producing areas that once were completely controlled by the six largest international companies.³⁵ The authors challenge the argument that the infinitely less costly and super-abundant reserves of the Middle East must be priced on the basis of Gulf of Mexico prices.

It is a sound economic principle that competitive market price must cover the highest cost increments of supply which are required within a given market area . . . [provided] that market supply be not expandible at any lower cost. It is idle

32. *Id.* at 363. The marketing subsidiaries of major companies are taxed at the regular 52 per cent rate. Production subsidiaries, however, get both percentage depletion and fast write-off of intangible drilling costs. This affords another reason to push for wide margins and stabilized profits in Crude. For an excellent discussion of the public policy considerations related to depletion, see Freeman, *Percentage Depletion For Oil—A Policy Issue*, 30 *IND. L.J.* 399 (1955).

33. DECHAZEAU AND KAHN 191.

34. *Id.* at 193.

35. For a vivid but at times rather loose discussion of the international oil companies see O'CONNOR, *THE EMPIRE OF OIL* (1955).

for the oil industry to parade Middle East prices as competitive in this sense as long as the expansion of supply from this area is limited by company policy rather than by cost.³⁶

Not only are the pricing policies of the international companies criticized but also the present system of incentives for foreign exploration is subjected to criticism.

The logic of the United States taxpayer offering special inducements to exploration abroad, which benefits primarily foreign consumers [because of import controls] and widens the gap between American and foreign price levels, can hardly go unquestioned.³⁷

The principal arguments in Part II are summarized as follows:

It is quite evident that for the international companies, if not for the majors generally, an increase in crude prices need be reflected very little indeed in product prices for them to benefit.³⁸

When product prices are weakening, the greater the self-sufficiency ratio of the integrated refiner, the more it will be in his interest to have the crude price hold firm. His losses will be greater, the greater the responsiveness of crude to product prices; and the situation that spells margin squeeze for the independent refiner is preferable to the integrated firm than regaining normal refinery margins at the cost of a crude-oil price decline.³⁹

In the absence of a strong bona fide crude buyer interest in the deliberations of public authority (*e.g.*, the Texas Railroad Commission), the cutbacks in production allowables to market demand at a high domestic price threaten not only a vicious upward cycle between prices and costs but also a decline in domestic exploration and development. . . .⁴⁰

Admitting that it would be "presumptuous" to claim that the analysis had "conclusively resolved any of the issues," the authors, however, pose six conclusions:

36. DECHAZEAU AND KAHN 216.

37. *Id.* at 217.

38. *Id.* at 223.

39. *Id.* at 225.

40. *Id.* at 229.

1. Prorating programs currently in force provide "neither the substance nor the scope of public control needed to protect the public interest."⁴¹
2. Massive vertical integration means a "dependable downward (that is, buyer) pressure on crude prices does not exist."
3. A federal law should be enacted requiring mandatory unitization of fields. No production controls should be permitted so long as production does not exceed MER.⁴²
4. Import quotas should be abolished. A tariff or a subsidy would be preferable to the present mandatory quota system which throttles competition at the supply level of the industry.
5. National defense arguments have been . . . "too long used, by indirection to justify the uncritical projections of the policies of the Texas Commission." All such arguments should be subjected to "critical review."
6. The problem is a national problem and must be solved at the national level.

In Part III and Part IV the authors do indeed forsake the "broad highway of historical precedent" to struggle through "more rugged and less certain terrain." The analysis becomes less sure and at times rather ephemeral. In large part this uncertainty is unavoidable for two reasons. First, it is rooted in the central problem confronting all investigators of this industry—a basic lack of complete and reliable data. Second, the authors are dealing with many issues which are simply not susceptible to quantitative measurement.

An attempt is made to segregate the advantages of integration which are "merely sources of strategic private advantage" from those representing "social" gain. The former type ". . . may end by denying the public the benefit of a wide range of competitive alternatives."⁴³

41. These conclusions are discussed *id.* at 250-56.

42. Unitization involves lumping all of the ownership interests so that the field may be operated with maximum efficiency. It avoids the great wastes associated with excessive drilling. MER represents the maximum efficient rate of recovery. This is a true conservation concept based on engineering-geological principles and does not include the "production-to-demand" feature usually found in state conservation statutes.

43. The "inherent weakness" of the arguments favoring integration is said to rest in the fact that "there is no available objective standard of the relative efficiency of integrated operations . . . in the limited markets of an industry dominated by majors. DECHAZEAU AND KAHN 268.

Only a few parts of the discussion may be considered here.

It is suggested that vertical integration has played a "more positive and creative role in the development of refining than of production technology." Innovations at the marketing level have in most cases started with independents. Integration, however, has contributed to the "progressive efficiency" and over-all "impressive performance record" of the industry.⁴⁴ Times change, however, and so do institutions.

Today, with major brands firmly established in the public eye and with customers highly sensitized to good service, it is extremely doubtful if the continuing emphasis on investment in retail distributive facilities by the majors contributes to the public good, or perhaps even to their own.⁴⁵

Thus one major conclusion is that the economic forces that at one time may have justified integration into the marketing level of the industry have declined in importance. The authors hasten to add that no "artificial prohibitions on integration into marketing should be imposed in our present state of ignorance." The opportunity to integrate vertically "in order to make a profit should not be denied."⁴⁶ Likewise the information is not available to prove "beyond cavil . . . that vertical integration is unnecessary for a socially desirable rate of investment in production; but the presumption established for it is strong."⁴⁷

As to the major's ownership of pipelines, at present the benefits of integration seem to outweigh the potential disadvantages.

Although the integrated ownership of pipelines may still permit the exercise of discriminatory power, it is our conclusion that the effect of integration on balance is to encourage rather than discourage desirable and speedy extension of pipeline investment.⁴⁸

In product markets the non-integrated refiners and marketers operate at many disadvantages relative to the majors. But in spite of this it is clear that:

[I]n existing oil product markets it is mainly the independent refiners and jobbers who exploit opportunities for price competition—opportunities often created by the imbalance of major companies themselves. . . .⁴⁹

44. *Id.* at 309.

45. *Id.* at 310.

46. *Id.* at 311.

47. *Id.* at 321.

48. *Id.* at 346.

49. *Id.* at 385.

Final product prices are an admixture of both "impersonal" competitive market forces "and industry composite judgment." But how are product prices affected by integration?

Neither the pipeline nor the massive forward integration into marketing during the twenties and early thirties were adequate to prevent the disruptive influence of uncontrolled, flush production of crude oil. . . . But vertical integration cushioned the impact on the integrated firm, provided a differential advantage . . . in comparison with the independent, and promised through price leadership and controlled, branded distribution in partially protected markets a greater price and profit stability than non-integrated firms could hope for.⁵⁰

The security of the majors, however, is far from complete.

The tendency for the competition between integrated companies in product markets to force them to give away the cost reductions integration makes possible is the important element of validity in the persistent complaints by independent refiners and marketers that majors use their profits from production and transportation to subsidize downstream competition.⁵¹

But it is strong enough to work hardships on independent refiners and marketers:

Since integration tends to insulate the posted price of crude oil from the influence of changes in demand, especially against a reduction, these changes are concentrated on the refining margin, more particularly on refiners in inverse proportion to their crude-oil self-sufficiency.⁵²

Price discrimination is an important feature of the competition at the wholesale and retail marketing levels of the industry. The authors are unable to reach a definite conclusion as to proper public policy in regard to this issue.

It is simply not always clear that price rivalry would be any less effective if major suppliers were forbidden to discriminate. Conceivably, price wars in this event would be diminished, or prove self-limiting rather than cumulative. But price wars are themselves a highly selective, unstable, and impermanent form

50. *Id.* at 432.

51. *Id.* at 451.

52. *Id.* at 463.

of price competition. They may be the best one can hope for within the oil market structure. On the other hand, to prohibit price discrimination in these circumstances could improve competitive opportunities for independents, and, if so, it could ensure a wider and more stable distribution of the benefits of price competition.⁵³

A continued decline in the position of the independent refineries could pose serious threats to the vigor of competition. But it is possible to explain this decline in terms of two conflicting theories—both of which are “convincing.” First, their attrition can be explained in terms of the survival of the fittest which is a process in the public interest. Secondly, it can be argued that certain strategic advantages held by the majors have eliminated them and this may not be in the public interest. Again, the key consideration is another variation of the central theme of the study.

Fabricators in other industries have some assurance that pressures on the prices of their products will be transmitted back to raw material levels, so that the independent enjoys some reasonable prospect of a remunerative margin. Crude oil markets are sheltered against such pressures.⁵⁴

Lastly turning to the status of independent marketers :

. . . [T]here has been no trend on the part of major companies either since 1936 or since 1946 away from distribution through independent marketers, branded and unbranded considered together. On the contrary, in both gasoline and heating oils, more companies increased than decreased their percentage of total sales through such distributors.⁵⁵

The authors conclude that beyond the crude level, the industry is “workably competitive” and has given a “favorable account of itself in both price and quality.” This optimistic judgment, however, “rests heavily not only on the evidence of continuing price competition but also on the apparent virility of the independent refiner and jobber.”⁵⁶ If the undesirable features at the production level of the industry can be removed or modified the rest of the industry should be left alone.

Like all studies dealing with such a controversial area, *Integration* has both strong points and weak points. On the negative side, the biggest

53. *Id.* at 481.

54. *Id.* at 512.

55. *Id.* at 535.

56. *Id.* at 563-64.

criticism is that the organizational outline of the book leaves something to be desired. It would appear that a tighter, more logically interconnected outline might have made reading easier, reduced the length, given a more convenient grouping of related materials, and perhaps avoided some of the repetitious material in the text.

Although *Integration* is carefully worded on the whole, in a few instances the authors use unqualified statements which no doubt will be quoted (and not completely out of context) to prove positions other than those the authors were actually taking. For example, in the general discussion of tax inducements this somewhat ambiguous sentence appears:

These tax inducements undoubtedly have the effect of enhancing the flow of capital into crude oil exploration and production and hence of holding the price of oil lower than it otherwise would be.⁵⁷

Obviously it can be argued that these same tax inducements also encourage the policies leading to high rigid prices for crude oil, of which the authors are so critical. In addition, the authors state:

An exploratory effort sustained by the lure of tax avoidance is likely to be socially wasteful. Special inducements to explore, drill for, and produce domestic oil; mounting capital outlays and higher costs in production; and prorationing restrictions on output that idle efficient production, lengthen the pay-out period and reduce the return on investment. There is a vicious circle here that must be broken. . . .⁵⁸

There is, of course, no way to demonstrate quantitatively whether the tax inducements have in the long run resulted in higher or lower prices for consumers.

On a few occasions the analysis seems to have missed some of the implications of the argument. For example, it was stated:

The greater the monopoly surcharges imposed on a product as it moves from one production stage to the next, the lower will be the costs of vertically integrated as compared with a non-integrated operation, and the greater will be the promise integration offers of low prices based on actual, rather than monopolistically inflated, costs of production.⁵⁹

57. *Id.* at 221.

58. *Id.* at 320.

59. *Id.* at 381.

As abstract theory this statement is sound if the word "promise" indicates potential rather than predicted performance. In the petroleum industry, however, if (as the authors contend) the main downward pressure on prices comes through the independents, is it not just as logical to argue that the wider the monopoly surcharges against the independents the less able they will be to compete and to exert effective downward pressure on prices? In other words, the opportunity for lower pricing by the integrated companies might be increasing at the same time the pressure on them to effectuate lower prices might be decreasing.

The important conclusion that independent marketers are holding their own—particularly in gasoline—is based on questionable evidence.⁶⁰ Trade sources and other studies indicate the following statements may be closer to the truth.⁶¹

1. Jobbers, both branded and private brand, have virtually lost their once lucrative commercial account business to their suppliers.
2. Gasoline jobbers, both branded and private brand, have lost position in major metropolitan areas due to the trend to direct selling.
3. Some of the ground lost in gasoline has been regained in fuel oil—particularly in rural areas.
4. Natural gas (owned mostly by the majors) in many areas is making inroads on the fuel oil business of independent marketers.
5. The current rash of acquisitions and mergers, the trend towards controlled distribution, toll roads and the new highway program, the increase of one-stop shopping centers, and other factors cloud the future for the independent marketer.

Virtually all of the majors have consistently refused to divulge data

60. *Id.* at 535. Questionnaires were sent to seventeen companies. Replies "in various degrees of usability" were received from eleven companies. The latest year for which data was requested was 1953. These results were lumped with a similar study made by McLEAN AND HAIGH, *op. cit. supra*, note 13. Strangely enough the figures given by McLean and Haigh show a definite decline in the percent of gasoline sold by wholesale resellers between 1946 and 1950. *Id.* at 444.

61. See Hewitt, *The Principal Factors Affecting Oil Marketing Now and Tomorrow*, National Petroleum News, December, 1959, p. 77. This is an abbreviated version but copies of the full article are available on request from National Petroleum News, W, 42nd St., N.Y. 36, N.Y. See also, Hewitt, *Summaries of Jobber Studies*, Hoosier Independent, May, 1959, p. 7.

concerning the jobbers and distributors with whom they deal. On this question as on most other critical questions concerning the industry, reliable complete information is simply not available.

For some, perhaps the most fundamental criticism that may be made of *Integration* lies in the assumption that approximately pure competition (meaning price competition) is *the* desirable goal of public policy. The late Professor Schumpeter of Harvard, and others have argued that some price inflexibility and monopoly may be necessary to encourage investment, long range planning, and scientific research.⁶² Indeed, some of the arguments here are recognized by the authors.

[I]ntegration sensitizes responses and diminishes the range of price inducements required. It introduces a kind of administered economy where the line is more nearly direct from anticipated demand to expanded supply with a lesser necessity for intermediate price fluctuations to induce the appropriate adjustments in the allocation of productive resources. To the extent that the integrated companies guess right, it would seem that they could accomplish the process more efficiently, with less delay, less price fluctuation, less possibility of alternating wasteful under and overinvestment than typifies free markets that depend more upon the lagging responses of investors to price movements.⁶³

Although the central conclusions relative to the crude level are convincing, it is difficult to predict how mandatory unitization and uncontrolled production up to MER would effect the various levels of the industry. Would crude prices really be more flexible? What would happen to nonintegrated independents if vigorous price competition developed at all levels?

On the asset side, by almost any standard *Integration* represents a major contribution. First, the analytical approach employed will make any fair minded reader more appreciative of the fact that there are no simple issues or solutions in this industry. Second, on many occasions the analysis breaks new ground. The basic conclusions reached are neither startling nor original; but the careful, and for the most part, con-

62. SCHUMPETER, *SOCIALISM, CAPITALISM AND DEMOCRACY* (3rd ed. 1950). John K. Galbraith cites the oil industry as example of how monopolistic elements can be highly innovative. GALBRAITH, *AMERICAN CAPITALISM: THE THEORY OF COUNTERVAILING POWER* (1952).

63. DECHAZEAU AND KAHN 262.

vincing arguments used give these conclusions added stature.⁶⁴ Every person interested in this vital industry should read this book. Both the authors and the American Petroleum Institute are to be congratulated for the parts they played in its production.

CHARLES M. HEWITT†

THE STATE LEGISLATIVE INSTITUTION. By Jefferson B. Fordham. Philadelphia: University of Pennsylvania Press. 1959. Pp. 109. \$2.75.

This slim little volume compiles three lectures that Dean Fordham gave at the West Virginia Law School in April 1957. Its slimness, fortunately, is no index of its significance. The main thesis lies in the first two lectures, which examine the present-day state legislature. A third lecture deals with the subsidiary question of legislative sanctions. I shall confine my comments largely to the first two.

It is not surprising that Fordham should find many inadequacies in the typical state legislature. What is surprising is the degree to which these inadequacies reflect a distrust of the practical workings of representative democracy. In a nation that professes so strongly its love of popular government it is remarkable how far the states have down-graded their legislative branches. Had the emergence of a strong Federal government meant a corresponding lessening of state responsibilities, this down-grading might not be significant. But the contrary is true: governmental responsibility has been increasing at all levels. All the more reason, then, to provide an adequate state legislative branch.

The biggest difficulty, says Fordham, is that in most states the legislature meets every other year and in many states only for periods limited by constitution. Special sessions are at the mercy of the governors, who alone can call them and prescribe the subjects that can be taken up. Legislative discontinuity is completed by the fact that between sessions even standing legislative committees have no legal status. The upshot is that the typical state has an inadequate main policy-making body in an era when the legislature has come to replace the court "as the prime agency of law reform" (p. 17).

64. For example, Rostow and Sacks, *Entry into the Oil Refining Business: Vertical Integration Re-examined*, 61 YALE L.J. 856 (1952). WHITNEY, *op. cit. supra*, note 6 suggested that crude production be related to MER. Virtually every disinterested scholar since John Ise wrote THE UNITED STATES OIL POLICY (1926) has suggested some changes for the production level of the industry.

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