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LEGAL METHODS OF PREVENTING BUSINESS CONSOLIDATIONS THAT REDUCE COMPETITION, WITH SPECIAL EMPHASIS ON THE AMERICAN EXPERIENCE

Remarks By

EDWARD T. TAIT
Federal Trade Commissioner
United States of America

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I. The Corporate System

Maintaining a climate favorable to the continued growth of our free enterprise economy while controlling excessive corporate power is the basic antitrust goal. The significance of the corporate concentration, which has existed in strategic sectors of the American economy for a number of years, is a much-debated and controversial issue. 1/ Recent figures show that in the third quarter of 1959, 130 corporations owned 50 per cent of the assets of the nation's manufacturing corporations. 2/

Concentrated corporate power raises unique problems in public policy. The corporate system has altered the structure of productive property. In pre-affluent society the entrepreneur owned and directed the use of mills, mines and land. In most large modern corporations, management has been separated from ownership. 3/ Since World War II the process of accumulating savings and stockholdings in pension trustees and insurance company managements tends further to divorce ownership from control of the mid-20th century corporation. 4/

Management control is now the locus of power in the bulk of American industries. 5/ Control in corporate law means the ability to elect the board of directors. Where there is no substantial minority interest and the stock is widely scattered among numerous stockholders, the capacity to direct the proxy machinery also maintains working control of the corporation. 6/

In classical economic theory the power of the corporate entrepreneur is restricted by decisions of the capital market to advance funds for plant expansion. Investors or investment banks could supplant inefficient managements by declining to provide capital. This force has been diminished. Major corporations primarily form their own capital through retained earnings. American non-financial corporations spent about $200 billion on capital goods and customer financing 1954 through 1959. Internal sources accounted for 70 per cent of these expenditures. 7/

Justice Brandeis called the corporation "a master instrument of American economy." As estimated by the Federal Reserve Board, corporate non-financial business in 1959 generated approximately $208 billion, over 50 per cent of total United States national income of $398 billion.

Political theories collide on the evaluation of corporate power. It has been suggested that the managers of great corporations will develop institutions expressing the corporate conscience as English royal power evolved equity procedures to reflect the king's conscience. 8/

The power of big companies is restrained, according to another highly theoretical argument, by the countervailing pressure of large customers and suppliers, including labor unions. 9/ Moreover, effective antitrust action can significantly reduce the extent of public measures to strengthen countervailing power.

Maintaining competition by means of antitrust laws is the American approach to the problem of concentrated power. 10/ Competition is the economic corollary of a political society in which governmental authority is diffused. Competition is an important element of our system of checks and balances. 11/ Departures from the competitive principle in our economic structure have been limited in scope, and competition remains the norm.

II. The Sherman Act and Integrated Industrial Combinations

In 1890 the federal government took the first step toward an explicit national policy on competition. The trust movement of the eighties grew out of the economic revolution and a period of cutthroat competition following hard upon the American Civil War. 12/ The corporate form of organization facilitated industrial consolidations. The downward trend of prices from 1865 to 1895, specially marked after 1873, put a premium on labor-saving machinery, new processes of manufacture, and on greater units of mass production. Corporations with large investments in plants slashed prices in depressed periods to cover heavy fixed costs. Competition appeared to threaten mutual destruction. Some businesses sought refuge in mergers and anticompetitive agreements.

A wave of trusts inundated industrial America in the 1880's. 13/ Organized agriculture and labor opposed business power over markets. The National Farmers Alliance and the Knights of Labor demanded governmental regulation of railways and curtailment of trusts. Edward Bellamy's Looking Backward, published in 1888, was a heavy gun in the

American literary war upon monopolies. His book envisaged the nation in 2000 A. D. as one great business corporation, employing industrial armies.

The construction of intercontinental railroads following the American Civil War welded the nation into one vast economic unit. Wave after wave of settlers seeking free public lands drove the frontier westward toward the Pacific Ocean. The frontier was a safety valve for economic pressures in the east. Frontier conditions fostered individualism and self-reliance in the American character.

The westward migration laid the groundwork for a great expansion of industry and commerce. With free land vanishing as the nation approached the closing decades of the 19th century, the economic independence of the individual was somewhat circumscribed. He could no longer load his wagon, hitch his horses and move. The passing of the American frontier made each American part of the nation's economic organization. He could no longer escape the direct effects of the actions of others. State legislatures began to react to the insistent demands of the American people for regulation of the industrial machinery.

The trust issue was forced into politics. By 1890, thirteen states had antitrust laws. 14/ The 1888 political platforms of both major parties pledged to curb the trusts. 15/ The United States Senate passed the Sherman Act with only one dissenting vote. The Senate bill was approved by the unanimous vote of the House of Representatives and signed by President Harrison on July 2, 1890. Truly such unanimity is unique in the politics of a democracy, and it reflects overwhelming concurrence by the public.

The central provisions of the Sherman Act 16/ are found in the first two articles. Section 1 prohibits "every" contract, combination or conspiracy "in restraint of" interstate or foreign commerce. Section 2 makes it unlawful to monopolize or attempt to monopolize such trade.

This law affirmed the philosophy of a competitive economy. The Supreme Court recently said in Northern Pacific Railroad Company v. United States: "The Sherman Act was designed to be a comprehensive charter of economic liberty aimed at preserving free and unfettered competition as the rule of trade." 17/

Congressional intent, as reflected in Senator Sherman's defense of his bill, infers the law applied "old and well recognized principles of common law" to combinations. But the common law has been described as a "metaphorical expression." 18/ There are many common law views. At first all contracts in restraint of trade were adjudged invalid at common law. The English courts came to distinguish between reasonable and unreasonable restraints of trade. 19/ Consequently, the Sherman Act was a ship sent out on a variously charted sea. The responsibility for selecting the course devolved upon the American courts.

The Supreme Court adopted the "rule of reason" as the criterion of Sherman Act legality in the Standard Oil case decided in 1911. 20/ Here are the main facts in that landmark case: From 1870 to 1882 Standard Oil Company acquired 90 per cent of the business of producing, shipping, refining and selling petroleum in the United States. By 1892 nine Standard Oil trustees controlled the stock of 84 companies. The specific act of combination after 1890 was the transfer of stock of 19 corporations to Standard Oil. To eliminate competitors, Standard Oil forced rebates from railroads, indulged in local price cutting, and operated bogus independent companies. The Court concluded that the combination was illegal under both the first and second sections of the Sherman Act.

As construed by this decision, the Sherman Act prohibited attempts to monopolize and unreasonable restraints on interstate trade. The resulting market position of Standard Oil created a prima facie case of intent to maintain dominancy over the oil industry. This presumption was made conclusive by Standard Oil's continued exertion of the market power acquired. The Court directed the corporation to return to the stockholders of subsidiary companies the stock which had been turned over to Standard Oil in exchange for its stock.

The Standard Oil ruling rests on the course of conduct of the persons and corporations involved. 21/ Combination of corporate entities was held not to be illegal per se. The Court stated: "And as the contracts or acts embraced in the provision [of the Sherman Act] were not expressly defined . . . it inevitably follows that the provision necessarily called for the exercise of judgment which required that some standard should be resorted to for the purpose of determining whether the prohibition contained in the statute had or had not in any case been violated." 22/

There appears as much judicial legislation in deciding that "restraint of trade" covered only unreasonable restraint as there was in prior decisions 23/ which said the Act covered all restraint. Under the rule of reason, the courts test combinations challenged under the Sherman Act in the light of specific wrongs, unreasonably restrictive acts, and illegal intent.

Monopoly entails the power to exclude competition. The existence of this power can be confused with proof showing monopolistic practices to control the market. In the 1920 United States Steel case the government failed to prove predatory practices from which the Court could infer the existence of monopolistic power. 24/ In 1945 Judge Learned Hand said in Alcoa, "It is no excuse for 'monopolizing' a market that the monopoly has not been used to extract from the consumer more than a 'fair' profit." 25/ By contrast, in the 1948 Columbia Steel case, the Supreme Court ruled that vertical integration, as such, is consistent with the Sherman Act unless the effects of such control "unreasonably restrict the opportunities of competitors to market their products." 26/

III. Mergers and Section 7 of the Clayton Act
(The words "acquisition" and "merger" are used synonymously although in United States corporation law they have different technical implications.)

Between 1900 and 1913 powerful new combinations were formed in steel, farm machinery, corn products, and in other major American industries. Sole reliance upon the Sherman Act seemed ineffective. In 1911 the construction of the Act in the Standard Oil case was reaffirmed in the American Tobacco case. 27/ Combinations that were not "unreasonable" would be allowed to stand.

In the 1912 Presidential election campaign, all three major political parties (Republican, Democratic and Bull Moose Progressive) urged some trade regulation legislation. The core of President Wilson's "New Freedom" was the protection of consumers from monopolies. Congress responded with the Federal Trade Commission Act and the Clayton Act. These measures were passed by substantial Congressional majorities and signed by President Wilson in 1914. Section 5 of the Federal Trade Commission Act prohibited unfair methods of competition in interstate commerce. The Clayton Act contained explicit but not absolute prohibitions against discriminations in prices, exclusive dealing and tying contracts, intercorporate directorships, and intercorporate stockholdings. These laws were designed to forestall the development of monopolies and restrictive practices by halting in their incipiency those practices which would, if allowed to continue unchecked, eventually violate the Sherman Act.

Section 7 of the Clayton Act prohibited stock acquisitions resulting in the substantial elimination of competition between any two corporate competitors in interstate commerce. Strict judicial construction confined the scope of this law. The Supreme Court held in 1926 that Section 7 did not apply to the acquisition of assets of competing corporations consummated prior to filing of complaint by the Federal Trade Commission. 28/

Mergers were common during the 1920's. The fields affected included public utilities and banking. The Great Depression of the thirties did not decentralize industrial control. In the early thirties the nation flirted with cartel acceptance through the NRA price stabilization codes later outlawed by the Supreme Court. During World War II the federal government coordinated industrial production through a hierarchy of primary defense contracts and subcontracts. After the war numerous combinations occurred in the food and beverage, textile, chemical and drug industries. From 1940 to 1947, more than two thousand corporations in mining and manufacturing disappeared through mergers. 29/ The Federal Trade Commission frequently urged Congress to amend the Clayton Act to cover acquisitions of assets as well as stock.

Section 7 of the Clayton Act was amended on December 29, 1950, primarily to stem the tide of oligopoly. 30/ The new section prohibits a corporation subject to Federal Trade Commission jurisdiction from acquiring the whole or any part of the stock or assets of another corporation where "in any line of commerce in any section of the country" the effect "may be substantially to lessen competition, or to tend to create a monopoly." The modified Section 7 is the primary law to which the Federal Trade Commission and the Department of Justice are resorting to contest the legality of mergers.

The amended Section 7 reaches beyond Sherman Act prohibitions. Historically speaking, the Sherman Act requires findings of actual anticompetitive effects. 31/ Section 7 covers mergers where there is the reasonable probability of the proscribed impact. 32/ Another purpose of Section 7 is to stop monopoly in its incipiency. Section 7 contemplates legal action at "any time when the acquisition threatens to ripen into a prohibited effect." 33/ The intent of the merging parties is not relevant to a showing of violation under Section 7. 34/

Delineating the Line of Commerce

The Section 7 test of illegality applies to "any line of commerce in any section of the country." The "line of commerce" denotes a product market and "section of the country" means a geographic market. 35/ In a merger case, therefore, the Commission or courts must decide the specific products or services affected competitively. It is then necessary to delineate a relevant geographic area for examining the competitive effects of the acquisition. These legal determinations are sometimes described as defining the relevant market.

The boundaries of the relevant market are crucial to the legality of mergers. Restrictive market definition may place the acquirer and acquired corporations in separate non-competitive product lines or sales territories. A broadly defined market covering a large territorial or product area may unreasonably dilute the market significance of the merged firms and, again, exonerate the merger. 36/

The product market was the controlling factor in the du Pont-General Motors decision in 1957. The United States Supreme Court held that a violation of the old or unamended Section 7 resulted from du Pont's purchase in 1917 to 1919 of a 23 per cent stock interest in General Motors. On the date of the Supreme Court's 4-2 ruling, du Pont held 63 million shares of General Motors' stock, worth $2.7 billion. 37/ The government charged that this vertical integration gave du Pont a preferential position with General Motors in the supply of automotive finishes and fabrics. Du Pont contended that the line of commerce was the total market, both non-automotive and automotive, for industrial finishes and fabrics. Under this defense concept General Motors claimed only 1.6 per cent of the fabric field and 3.5 per cent of the market for finishes sold to industrial users.

The United States Supreme Court rejected the broad defense definition of the product market. It declared that automotive finishes and fabrics have "sufficient peculiar characteristics and uses" to make them each a "line of commerce." 38/ The demand for these materials is derived from the demand for automobiles. General Motors accounts for almost a majority of the annual sales by the automobile industry. The majority opinion reasoned that General Motors' requirements for automotive finishes and fabrics must also represent about 50 per cent of the relevant market.

In late 1957 the Federal Trade Commission issued an order, now on appeal in the courts, which requires Crown Zellerbach Corporation to divest itself of St. Helens Pulp & Paper Company. 39/ Crown ranks as one of the nation's largest producers of paper and paper products. Crown's integrated timber, pulp, paper manufacturing and conversion operations are located in the States of Washington, Oregon and California. During 1953 Crown acquired substantially all of St. Helens' stock valued at about $9,557,000. St. Helens was a fully integrated paper manufacturer located in the State of Oregon. St. Helens produced and sold primarily bleached and unbleached kraft papers. The Commission decided that Crown-St. Helens merger contravened Section 7 of the Clayton Act.

The line of commerce was a bone of contention in the Crown case. Crown argued that the product market encompassed trade coarse paper and paperboard, including container board. The Commission determined that the relevant line of commerce was coarse paper relating generally to coarse wrapping papers, bag and sack papers, and other converting papers. These coarse papers, the Commission said, are "in a relatively allied line, particularly in respect to markets and end uses." The Commission excluded container board from the product market since container board is used in the manufacture of paper boxes and it is ordinarily a heavier paper than wrapping and bag papers. Similarly, the Commission stated in the Brillo case that the "physical characteristics" of the products are among the factors determining the extent of the product market. 40/

The product sold to distinct customers may indicate a separate line of commerce even if machines making the product can be shifted to other lines. 41/ Specialized investment, as required in steel manufacture, is among the criteria used to determine whether the iron and steel industry is an appropriate product market. 42/ The existence of a trade association is another element that may help determine that a given product or products constitute a "line of commerce" for amended Section 7 purposes. 43/

Substitute products may be considered within a single line of commerce when purchased by substantial classes of purchasers for similar uses. But product interchangeability is not a necessary test of a single product market. In the Cellophane monopolization case, the Supreme Court decided in 1956 that the line of commerce was flexible packaging materials rather than cellophane. 44/ Du Pont accounted for 75 per cent of the nation's cellophane. But cellophane was less than 20 per cent of the broader flexible packaging field. The subsequent Bethlehem decision 45/ distinguished the du Pont Cellophane case as applying to the monopolization charge of Section 2 of the Sherman Act while acknowledging the high degree of interchangeability referred to as a test by the Second Circuit Court of Appeals in the American Crystal Sugar case. In the Section 7 case against American Crystal Sugar, the Court decided that cane sugar and beet sugar comprised a single refined sugar market. 46/

The Court ruled in American Crystal Sugar that a cane sugar producer violated Section 7 by acquiring stock control of a beet sugar refinery. Apparently the Court relied on the "cross elasticity of demand" concept to specify refined sugar as the line of commerce. Cross elasticity of demand is the extent to which the demand for one commodity responds to changes in the price of another product. In American Crystal Sugar the Court noted: "To establish that for consumer purposes cane and beet are not interchangeable, it would be necessary to show that within a given range of prices consumers would not shift from one to the other." 47/

The market test proposed in a recent Virginia Law Review analysis reasons: "If, within this purported market, prices were appreciably raised or volume curtailed, would supply enter in such amounts as to restore approximately the old price and output? If the answer is 'yes,' then there is no market, and the definition must be expanded. If the answer is 'no,' the market is at least not wider." 48/

In the Bethlehem case the Court said: "There can be a substantial lessening of competition with respect to a product whether or not there are reasonably interchangeable substitutes." The Court added, however, that interchangeability cannot be ignored. 49/ Champagne and Poland Spring water are not competing products, although substitute thirst quenchers. The clause "line of commerce" should not be so broadly construed as to defeat its economic purpose.

The market concept in Section 7 has a functional dimension. Du Pont's preeminent position with General Motors narrowed the General Motors' market for other producers of automotive finishes and fabrics. Similarly, the functional market was a significant element for measuring market control in the Federal Trade Commission's Spalding ruling in March 1960. 50/ This decision held illegal the acquisition by A. G. Spalding & Co. of Rawlings Manufacturing Company. Both Spalding and Rawlings produced primarily athletic goods in the higher priced quality lines. The Commission differentiated low priced athletic items not suitable for use in organized sports, and the higher quality and higher priced athletic products designed for use by professional and amateur teams. It held: "The products in each of these categories are physically distinct from those in the other; they are different in quality and price, as well as in the purpose for which they are made and used." 51/

Dimensions of the Geographic Market

In Section 7 litigation the burden is on the government to sustain the "line of commerce" and "section of the country." The relevant area will vary with the product. Jeweled watches are sold in a national market. 52/ Lake sand is distributed within a region extending ten to twelve miles inland from Lake Erie. 53/ Local markets are involved in shoe retailing. 54/ The geographic market may coincide "with a political subdivision, a combination of states or the nation." 55/ It is determined, however, by economic realities rather than legal abstractions or political boundaries.

Market boundaries are acute factors in particular merger cases. The combined firms' market shares are reduced by enlarging the common sales area. Conversely, the respondent may attempt to place the merged producers in separate markets. This checkmates the government contention that increased market shares accrue to the acquirer in the pertinent sections.

The Crown decision found that the eleven western states of the United States were an appropriate area for the product market. The merged producers each made over 80 per cent of their domestic sales in that region. Imports of the relevant papers in the area were relatively insignificant due to the preference of purchasers and high freight charges. 56/ In Bethlehem, higher freight rates for Bethlehem Steel Corporation than for Youngstown Sheet and

Tube Company did not justify separation of eastern and mid-continent steel markets. The significance of freight costs "depends not on their existence or their size, but on how they function and the extent to which they operate to insulate buyers and sellers in one area from buyers and sellers in another." 57/

In the Bethlehem decision the Court prevented the proposed merger of the nation's second largest steel producer (Bethlehem) with the fifth largest (Youngstown). The acquisition would have increased Bethlehem's share of the steel industry's ingot capacity from about 16 per cent to 21 per cent. The combined firms' annual capacity of about thirty million tons of steel compared with about forty million tons for United States Steel Corporation, the nation's number one steel producer. The merged assets would have totaled close to $3 billion, as compared with U. S. Steel's $4 billion.

The Court in Bethlehem pointed out that twelve integrated steel producers control about 83 per cent of the industry capacity. Section 7 is contravened, the Court decided, when concentration is substantially increased by merger, or when a substantial competitive factor is eliminated. The defense had argued that the Bethlehem-Youngstown amalgamation would offer more challenging competition to U. S. Steel. The Court disagreed: "The merger offers an incipient threat of setting into motion a chain reaction of further mergers by the other but less powerful companies in the steel industry. . . ; and so we reach a point of more intense concentration in an industry already highly concentrated--indeed we head in the direction of triopoly." 58/

According to the defense market theory in Bethlehem, the United States is divided into three steel markets: Eastern, Mid-Continent, and Western. Bethlehem Steel Corporation is in the Eastern market, with plants at Bethlehem, Johnstown and Steelton, Pennsylvania; Sparrows Point, Maryland; and Lackawanna, New York. Bethlehem also operates in the Western market with plants on the Pacific Coast. The East Chicago plant of the Youngstown Sheet and Tube Company is within the Mid-Continent market. Youngstown had another facility in the Pittsburgh-Youngstown-Cleveland production center. The Court said that the defendant's tripartite division of the nation was market gerrymandering, since the merging producers shipped substantial steel tonnage to distant consumers by resorting to freight absorption.

The Court in Bethlehem adopted as areas of effective competition the whole United States, certain states separately, and a quadrant of states. It was not doubly contradictory to partition the area into separate states and make findings relative to them. The law is designed to protect competition in "any" section of the country. The particular merger may have substantial impact on several areas.

The appropriate locale may be where the acquirer or acquired do business, but Section 7 is also "broad enough to cope with a substantial lessening of competition in any other section of the country as well." 59/ The market determination normally is made on the basis of both the actual and potential sales areas of the merging corporations. 60/ The Court said: "Section 7 is intended to protect buyers as well as competing sellers. Therefore, 'section of the country' must be determined with respect to both buyers and sellers. The determination must be made on the basis of not only where the companies have in the past made sales, but also on the basis of where potentially they could make sales and where buyers could reasonably turn to them as alternative substantial sources of supply."

Criteria of Competitive Effects

Once the relevant market has been determined, the Commission or courts must next assess the probable competitive consequences in the delineated market. Before illegality obtains, the threatened lessening of competition must be "substantial" or the necessary tendency toward monopoly must be shown. The recent Commission decision in the Spalding-Rawlings merger provides guidelines for appraising market effects. 61/ In 1955 A. G. Spalding & Bros., Inc., acquired all of the capital stock of Rawlings Manufacturing Company for approximately $5.7 million. Spalding ranked second and Rawlings fourth among the nation's producers of athletic goods.

The high-priced line of athletic goods constituted a line of commerce. The decision adopted the entire nation as the appropriate geographical market. On a value basis Spalding controlled 21.8 per cent of the baseball producing market and the acquired Rawlings had 11.3 per cent. The Commission said that the merger eliminated a major competitor. The merger combined the second and fifth ranking baseball producers to make Spalding the largest producer with

33.1 per cent of the market. Spalding's market shares were also significantly enhanced in higher-priced basketballs, footballs, and softballs.

The Spalding opinion stressed the relative fewness of major companies in the concentrated relevant markets. Before the merger, only four firms--Spalding, Rawlings, Wilson and MacGregor--produced and sold a general line of athletic products. When Spalding absorbed Rawlings, the three remaining firms accounted for almost 50 per cent of total industry production. The Commission contrasted the large disparity in sales volume between the market leader and other competitors. Spalding's post-merger sales were more than four times that of the fifth ranking firm. Moreover, the smaller firms operate mainly in the low quality field of athletic merchandise. The union of Spalding and Rawlings greatly increased concentration in the higher quality lines.

The Commission considered the possibility of new competitors replacing Rawlings. It found the likelihood of sustained entry remote. Spalding has a long term contract to supply both major professional baseball leagues with its baseballs until 1966. In 1954 the four leaders had exclusive contracts to supply baseballs to 89 per cent of the minor professional baseball leagues. Endorsement contracts with prominent athletes as well as national advertising, patents, and facilities and resources for research and development contribute significantly to the competitive lead of the general athletic lines producers. These advantages, the Commission observed, present "formidable barriers to effective competition from new entrants in the field or from firms now in existence." 62/

Where the relation between merging corporations is vertical (manufacturer and customer or raw material producer and manufacturer), the merger may cut off concerns with which one of the merging units did business. The big integrated producer in concentrated fields may have the power to squeeze competitors. The extent to which such power has been used is a question for the research economist. As a raw materials supplier the large integrated operation may be able to charge high prices for materials and low markups above these prices in its own sales of processed products. By this strategy it may reduce the profit margins of its customer-competitors who pay high prices for basic materials and receive relatively low prices for finished goods. As a purchaser it may follow the reverse policy.

The integrated giant may be able to hold down the price of raw materials which it both produces and buys and increase its operating margin on the finished products. 63/ The thrust of Section 7 invalidates mergers that foreclose or narrow substantial sources or outlets. 64/

This principle is explicit in the Spalding decision. Prior to the Spalding-Rawlings merger, Rawlings purchased its requirements of nine products, including golf and tennis equipment, from Spalding and other producers. The merger foreshadowed potential competitive injury to former Rawlings' suppliers. The Commission declared: "By acquiring Rawlings, Spalding can, if it so desires, prevent other firms that manufacture these products from selling to Rawlings and thus cut off an important outlet for their merchandise. That there is a reasonable probability that this may occur is evidenced by a pre-merger announcement by Spalding that 'where possible and practical, as much of both lines will be manufactured in Spalding's and Rawlings' factories as seems appropriate.'" 65/

This merger virtually eliminated competition among manufacturers in the sale of higher-priced baseball gloves and catchers' mitts to Spalding. The Commission ruled that this significant fact would not be altered even if there had been testimony at the hearings that Spalding's competitors, Wilson and MacGregor, had not been adversely affected by the merger. 66/ Section 7 relates to "lessening of competition and not to injury to competitors." 67/

The Commission's decision in Farm Journal considered the possibility of the acquirer's market dominance. "Farm Journal" ranked as the largest national general interest farm magazine. The acquired property, "Country Gentleman," was second largest. The acquisition made "Farm Journal" the dominant farm magazine, circulation-wise, in many states." 68/

Strengthening the acquiring unit's already dominant position was cited by the Court as one of the consequences of the acquisition of the Embassy Dairy by the Maryland and Virginia Milk Producers Association. The acquirer-association acted as the marketing agency for almost two thousand farmers. It accounted for 86 per cent of fluid-milk sales to dairies in the Washington Metropolitan area. Embassy Dairy, fourth largest in the area, procured its milk supply from independent farmers who did not sell to the defendant association. The Court concluded that the acquisition violated Section 7. It said, inter alia, that the association "enhanced its dominating position in the market, even though it did not attain complete control." 69/

The facts in the Brillo case provide a useful context to interpret the meaning of "substantiality." In 1955 the Brillo Manufacturing Company, Inc., acquired all of the capital stock of the Williams Company. Five other producers besides Brillo and Williams sold steel wool nationally in the industrial steel wool market. Brillo controlled 29.1 per cent of this market in which it was the largest producer. Williams was fourth largest in this line, with 18.2 per cent. In the household steel wool market, Brillo held 45.3 per cent of sales and ranked second compared to SOS with 50 per cent. Williams had 0.3 per cent of this market. Regarding the household market, the Commission concluded: "It therefore is not controlling that the share held by Williams was a fraction of one per cent. The Act also encompasses minute acquisitions which tend to monopoly." 70/

There are sound economic and legal grounds for the Brillo thesis. "Substantiality" should not be defined solely by the amount of change in market structure resulting from an acquisition. Under such a restricted view, a merger that changes a competitive market into one moderately competitive would properly be held illegal, while paradoxically a merger which took a seriously uncompetitive market and made it slightly less competitive would be valid. This follows even though the latter merger in the concentrated line would be more harmful than that of the indicated former acquisition which altered the competitive field. 71/

Viewed in the light of the facts in the Brillo case, the failure of theories of Section 7 illegality to include the merger where undue concentration is slightly increased is illogical and appears inconsistent with legislative intent. One major Congressional objective of the amended Section 7, as restated in Bethlehem-Youngstown, is "to ward off the anticompetitive effects of increases 'in the level of economic concentration resulting from corporate mergers and acquisitions.'" 72/ Accordingly, substantiality may be decided in an existing oligopolistic framework by the intensified concentration after the merger. In other cases it might be determined by the expected change in competitive activity flowing from an acquisition.

Undue concentration of economic power impairs the functions of competition. With few sellers, the buyer is faced with fewer alternatives of business policy. With fewer minds to synchronize, restrictive agreements are facilitated in oligopolistic markets. The damage to competition effected by concentrated economic power "is less revocable and potentially more extensive than that done by restrictive agreements." 73/ Conflict of interests among cartelists may upset restrictive agreements, but large enterprises, once established through mergers, are relatively stable organizations.

Tests as to general competitive conditions may also be applied to gauge the effects of mergers. The Brillo decision stressed Brillo's price leadership in the concentrated industrial steel wool field. 74/ In the Embassy Dairy case, the acquired dairy represented an active cut-price source of milk. The Court cited a memorandum from the acquirer's files which stated, in part, the benefits expected from the acquisition as follows:

"1. Elimination of bootlegging, i.e., bringing in cheap uninspected 'distress' milk from other markets.

"2. The elimination of this 'bootleg' milk will allow our own milk to replace it, to the great increase of the blend price." 75/

The Brown Shoe decision in 1959 analyzed the factors which the District Court weighed in reviewing the impact of the proposed merger of Brown Shoe Company and G. R. Kinney Company, Inc. The government sought injunctive relief to restrain the merger. The Court decided the combination of Brown and Kinney shoe manufacturing-retailing facilities would substantially lessen competition and tend to create a monopoly in the manufacture of "men's," "women's," and "children's" shoes, considered separately, in the nation as a whole. It also held these adverse effects would occur in manufacturing-retailing and in retailing alone in the indicated shoe lines in local common markets.

On market share control and criteria of merger illegality, the Court in Brown Shoe declared: "What difference can it make that Brown has only 5 per cent of the shoe production and Kinney 0.5 per cent, when Brown is the fourth largest (shoe) firm in the United States and Kinney with only 0.9 per cent of all retail shoe sales is the largest family shoe chain retailer. Their combination moves Brown to third place in the industry. Does it then make sense to say that this is imperceptible because the percentages are small?" The Court pointed out "that regardless of percentages or size, the test is, what do the facts show as to the trends in the industry and the true economic impact of this particular merger . . ." 76/ The Court referred to the definite trend in the shoe industry of manufacturers obtaining retailing outlets and increasing the sale of their own manufactured shoes to the acquired outlets. The Brown Shoe-Kinney union occurred in an industry with a few large firms holding a sizeable share of the total shoe output. The balance of production is divided among numerous others having only minute segments.

Containment of substantial conglomerate mergers is the new frontier in antitrust law. The amended Section 7 is intended to reach any purchase of stock or assets having the prohibited competitive effects. 77/ The conglomerate merger involves the purchase of an unrelated business. For example, during 1959 the nation's largest carbon dioxide producer acquired the largest producer of sand, gravel and concrete in the Chicago area.

Conglomerate mergers, as such, do not increase concentration in any line of commerce or decrease the number of market participants. But the conglomerate merger may support below-cost competition, other predatory policies or acquired competitive advantages from general revenues until the acquired concern drives out single market competition. 78/ New legal theories and economic evidence may emerge during the 1960's in Section 7 conglomerate cases.

IV. Merger Investigations and Enforcement

The Federal Trade Commission and the Department of Justice have pre-merger clearance programs. Liaison with the Justice Department avoids duplication of our investigative work. There is no legal requirement that merging companies notify us of the merger, either before or after the consummation. The decision to submit merger plans and request the Commission to clear proposed mergers lies within the discretion of the merging parties. On the data submitted, and other available information, the Commission informs the applicant whether it presently intends to take further action on the proposed merger. The statement of intent is not binding and it does not bar a later legal action. The Commission has not challenged a merger for which pre-merger clearance had been given. 79/

The Commission has no authority to obtain a court injunction to prevent completion of planned acquisitions or to preserve the status quo after completion of the merger and during pendency of a proceeding before us. 80/ The Department of Justice has this merger preventative power derived from Section 15 of the Clayton Act.

The adequacy of investigatory processes may make or break antitrust enforcement programs. The Commission can subpoena documentary evidence from any corporation under investigation. 81/ The agency often gets copies of all records, papers and information in the possession of government units pertaining to any corporation subject to jurisdiction. 82/ It can also compel a company to produce documents even though that concern is neither under investigation nor being proceeded against. 83/ This power allows the Commission to obtain market share statistics and other competitive data from competitors of merged corporations in Section 7 proceedings.

The Justice Department cannot employ compulsory process during the investigative stage in which civil antitrust proceedings are contemplated. It can file a civil complaint and then resort to discovery processes, 84/ or it may use information secured by a grand jury.

The Commission can order divestiture based on power derived from Section 11 of the Clayton Act. In Reynolds Metals the Commission's denial of petition to reopen proceedings stated: "The fact is that respondent was shown at the time of the hearings to be in violation of Section 7. This requires an order of divestiture under the statute. Even though subsequent events may show that future competitive conditions are not as anticipated, this would not make legal that which was illegal, nor relieve the respondent of the consequences of its action, unlawful as of the time of trial." 85/ The Commission has authorized partial divestiture in certain consent settlements. 86/

Counting only those cases within its jurisdiction, the Federal Trade Commission recorded 1050 acquisitions in the calendar year 1959. This compares with 899 in 1958 and 941 in 1957. Manufacturing and mining acquirers with assets of $50 million and over accounted for 41 per cent of the 1959 merger total. Acquiring concerns in these industries with assets of $10 million to $50 million made 32 per cent of the 1959 mergers. 87/

In the United States today there is no evidence of Congressional intent to use major surgery on our anti-merger laws. Both major political parties support these laws. The antitrust laws are generally effective. Present administration of the anti-merger laws has been resolute, consistent with Congressional intention, and in accordance with our principles of due process of law.

Legislative antitrust revisions presently being considered aim to ease antitrust administration and assure more effective remedies. In the Economic Report of the President transmitted to Congress on January 20, 1960, President Eisenhower requested Congress to take four specific actions to strengthen competition. These recommendations follow:

> "The first would require that antitrust agencies be notified when firms of significant size engaged in interstate commerce propose to merge. The second would authorize the Federal Trade Commission to seek preliminary injunctions in merger cases where a violation of law is likely. The third would strengthen Federal law governing bank mergers accomplished through the acquisition of assets. The fourth would grant the Attorney General power to issue civil investigative demands under which the necessary facts may be elicited when civil procedures are contemplated in antitrust cases." 88/

The foregoing discussion and cases disclose the accumulated pattern of Section 7 interpretation to date. This antitrust law must be applied prospectively. Its basic principle is that the nation's economic welfare is best served by maintaining competition. Anti-competitive consequences arise from a serious reduction of competitive opportunities or impairment in the incentives to compete. 89/ Judgments as to competitive effects of the challenged merger should focus on reasonably probable changes in market structure and competitive behavior in the relevant markets.

The effectiveness of the anti-merger laws should not be measured solely by the number of proceedings instituted. These laws have been a barrier against the cartelization of American industry. Without these laws there doubtless would be more mergers. The very fact of their existence and enforcement provides a significant deterrent effect. 90/ From our experience it appears that fewer significant horizontal mergers have been consummated in recent years. These laws help to maintain competitive opportunities and freedom of access to markets. Thus we have a method of controlling excessive corporate power while at the same time permitting the continued growth of a free enterprise economy in our country.

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2. Federal Trade Commission, Quarterly Financial Report for Manufacturing Corporations, Third Quarter, 1959, pages 50, 54 and 55. The basis of the calculation follows:

Financial Statement For All U.S. Manufacturing Corporations, By Asset Size

Assets	All Asset Sizes, U.S. (3rd Quarter 1959, Million Dollars)	$250 Million and over (130 corp.) (3rd Quarter 1959, Million Dollars)	%
Total cash and U.S. Government Securities	28801	14455	50
Total receivables	38609	14017	
Inventories	55796	23461	
Other current assets	5351	2773	
Total current assets	128557	54706	
Total property, plant, and equipment (net)	92596	53410	58
Other nonrecurrent assets	18854	11488	
Total assets	240008	119606	50

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7. The data were derived as follows:

Sources and Uses of Corporate Funds in U.S., 1946-1953 and 1954-1959.

	In Billions of Dollars 1946-53	1954-59
Expenditures by Nonfinancial Corporations		
Plant, equipment, and changes in inventories	166	168
Trade credit	27	30
Consumer credit	4	2
Total, capital expenditures and customer financing	197	200
Sources of Financing		
Retained earnings	141	159
Minus lending	-15	-18
Internal financing	126	141
External financing	71	59
Corporate bonds	24	26
Corporate stock	12	13
Other	35	20
Total, internal and external sources	197	200

Source: Federal Reserve Bulletin, August 1959, page 1050, and unpublished data from Flow of Funds Section of the Board of Governors of the Federal Reserve System.

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