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NOTES AND COMMENTS

CORPORATE ACQUISITION OF DISTRIBUTIVE FACILITIES

Although nothing of consequence has developed in the general law of corporations bearing on the right of one entity to acquire the distribution facilities of another by the simple process of acquiring the stock or assets of the second corporation, hardly a day goes by in which some corporation lawyer is not faced with a question as to whether such an acquisition would produce a violation of Section 7 of the Clayton Act.[1] For that matter officers of thriving manufacturing enterprises, desiring to expand, to out-sell their competitors, to control more closely the process of distribution of their products, and, ultimately, to earn more profits by a reduction of expenses through volume sales, are also daily facing that question. But, while a clear, definite answer as to the legality of such acquisitions would remove much of the hesitancy and lend a degree of certainty to future planning, there is no one answer for two conflicting schools of thought exist over the question. One such school is represented by the opinion of the United States Supreme Court in the case of *Standard Oil Company of California* v. *United States*,[2] which opinion, together with the commentaries of the advocates of its soundness, constitutes what may, for convenience, be called the Standard Stations doctrine. In opposition thereto, is the view more recently enunciated by the Federal Trade Commission in the matter of *Pillsbury Mills, Inc.*,[3] which view has found support in certain of the commentaries written thereon. The presence of these two views invites a re-examination of the legal complexities likely to arise under federal law in an area where state law would present no problems.

In that connection, it might be noted that the Standard Stations case grew out of a suit brought by the United States under Section 1 of the Sherman Act and Section 3 of the Clayton Act[4] to enjoin a major oil

[1] 15 U. S. C. § 18 declares, in part, that no "corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital and no corporation subject to the jurisdiction of the Federal Trade Commission shall acquire the whole or any part of the assets of another corporation engaged also in commerce, where in any line of commerce in any section of the country, the effect of such acquisition may be substantially to lessen competition, or tend to create a monopoly."

[2] 337 U. S. 293, 69 S. Ct. 1051, 93 L. Ed. 1371 (1949), affirming 78 F. Supp. 850 (1948). Douglas, J., wrote a dissenting opinion, as did Jackson, J. Chief Justice Vinson and Burton, J., concurred with Justice Jackson.

[3] F. T. C. Docket 6000 (1953).

[4] 15 U. S. C. § 14 states that it "shall be unlawful for any person engaged in commerce . . . to lease or make a sale or contract of sale of goods, wares, merchandise, machinery, supplies, or other commodities . . . or fix a price charged

company and its subsidiary from entering into or enforcing exclusive supply contracts with independent dealers of petroleum products and automobile accessories. The parent company was the largest seller of gasoline in a seven-state market area[5] and had operated under a system of requirement contracts[6] similar to those used by its major competitors. The Justice Department argued that the facts were sufficient enough to support a conclusion that the effect of these contracts, in the language of Section 3, could be "to substantially lessen competition." By contrast, the company claimed that, in actuality, the contracts had not lessened competition, and it sought to offer evidence to show the general economic picture within the industry. The trial court held that the need for showing an actual or potential lessening of competition, *i. e.*, a tendency to establish monopoly, had been adequately met by proof disclosing that the contracts covered a substantial number of outlets and a substantial amount of products, whether considered comparatively or not, so it granted the declaratory relief sought.

When Standard appealed to the federal Supreme Court on the issue as to whether or not the requirement of a showing that the arguments could potentially "lessen competition" had been met simply by proof that a substantial portion of that commerce was concerned, the court answered in the affirmative, thereby upholding the decision of the lower court. Holding this "quantative substantiality test" to be a proper one, the majority of the court rejected the assertion that the government had to demonstrate that competitive activity had actually diminished or probably would diminish, thereby indicating that the qualifying clause of Section 3 would be satisfied by proof that competition had been foreclosed in a substantial share of the line of commerce affected. Exclusion of evidence as to economic factors was said to be proper on the basis the same was immaterial for, admitting that control of distribution would be likely to result in a lessening of costs and that the abandonment thereof

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therefor . . . on the condition . . . that the lessee or purchaser thereof shall not use or deal in the goods . . . of a competitor . . . where the effect of such lease, sale, or contract of sale . . . may be to substantially lessen competition or tend to create a monopoly in any line of commerce."

5 In 1946, 23% of the total taxable gallonage sold in the market area was accounted for by Standard Oil; with sales through company-owned service stations constituting 6.8%, and sales under requirements contracts with independent service stations constituting 6.7% of that total. The remainder was sold to industrial users. Standard Oil and its six largest competitors sold 42.5% of all the gallonage in this area.

6 Standard Oil had such contracts with 16% of all the retail outlets in the area. Through them, the company sold nearly $58,000,000 worth of gasoline, and a little over $8,200,000 worth of other products, of which tires and batteries never exceeded 2% of all sales in the area. During the ten-year period prior to 1946, Standard Oil's proportionate sales of gasoline had remained at a stand-still but its sales of lubricating oils had dropped from 6.2% to 5% of the total.

could increase costs, under the interpretation given to Section 3, such a consideration was not a proper one to be taken into account. For that matter, the company's defenses that competition had actually increased, that its sales had declined, and that its competitors were engaging in the same type of activities, while regarded as important factors in an economic analysis of the situation,[7] were also said to have no bearing on the legal implications.

It was in relation to those same legal implications that the majority of the court placed great emphasis on the legislative history of Section 3. Noting that that section had originally passed the House as a *per se* prohibition, and that the qualifying "competitive impact" clause had not been added until the bill reached the conference stage, the court considered it significant that the "conferees responsible for adding that language were at pains, in answering protestations that the qualifying clause seriously weakened the section, to disclaim any intention seriously to augment the burden of proof to be sustained in establishing violation of it." It was also the view of the majority of the justices that it could hardly seem likely that, "having on one hand set up an express prohibition against a practice thought to be beyond the reach of the Sherman Act, Congress meant, with the other hand, to re-establish the necessity of meeting the same tests of detriment to the public interest as that Act had been interpreted as requiring." Such being the case, to insist upon an investigation of that type would be "to stultify the force of Congress' declaration that requirements contracts are to be prohibited wherever their effect 'may be' to substantially lessen competition."[8] In brief, therefore, it seemed to be the majority view that Section 3 served, if not entirely, then at least very nearly as a *per se* prohibition of exclusive dealing agreements.

It should, in fairness, be said that the court recognized that if the Clayton Act were to be administered solely by the Federal Trade Commission there might be good reason for the establishment of a test of violation which could take into consideration a myriad of economic factors but, as violations of the statute could also be litigated in the federal court system, a practical test had to be recognized. Justice Frankfurter expressed the thought by saying: "The dual system of enforcement provided for the Clayton Act must have contemplated standards of proof capable of administration by the courts as well as by the Federal Trade Commission and other designated agencies . . . Our interpretation of the Act, therefore,

[7] The court, in reaching its decision, did examine at least a part of the economic picture, to-wit: the dominant industry position of the company in the market area.

[8] 337 U. S. 293 at 312-3, 69 S. Ct. 1051, 93 L. Ed. 1371 at 1385-6.

should recognize that an appraisal of economic data which might be practicable if only the latter were faced with the task might be quite otherwise for judges unequipped for it either by experience or by the availability of skilled assistance."[9]

Those who advocate the application of the Standard Stations doctrine to matters falling under Section 7 of the Clayton Act derive support from two sources, to-wit: (1) the history of the application of unamended Section 7, known to Congress, and (2) the legislative history of the amendment to Section 7. The particular provision,[10] as framed at the time of the original passage in 1914, had been inspired by a spread of corporate mergers occurring at about the turn of the century and an apparent inability on the part of the government, acting under the Sherman Act,[11] to cope effectively with the problem. Its primary purpose, therefore, was to prohibit certain trade practices which were not covered by the Sherman Act and also to arrest the creation of monopolies in their inception and before their consummation.[12] However, the provision did not accomplish as much as was hoped for and, prior to the 1950 amendment, it had been an ineffective restraint on corporate mergers. One of the principal factors for this ineffectiveness was the obliteration of a distinction between standards of illegality under the two statutes. As a literal reading of original Section 7 would have required the conclusion that every stock acquisition between two competitors would be unlawful, the courts read into the original section a test which looked to the effect of the acquisition on competition in the industry as a whole, thereby requiring a showing of prejudice to the public interest akin to the "rule-of-reason" test which had obtained under the Sherman Act.

A leading example of this testimony may be found in the case of *International Shoe Company* v. *Federal Trade Commission*[13] where it was said that a mere "acquisition by one corporation of the stock of a competitor, even though it results in some lessening of competition, is not forbidden; the act deals only with such acquisitions as probably will result in lessening competition to a substantial degree . . . that it to say

[9] See footnote 13 at 337 U. S. 293 at 310, 69 S. Ct. 1051, 93 L. Ed. 1371 at 1384.

[10] See Act of Oct. 15, 1914, c. 322, 38 Stat. 731. It declared: "No corporation engaged in commerce shall acquire, directly or indirectly, the whole or any part of the stock or other share capital of another corporation engaged also in commerce, where the effect of such acquisition may be to substantially lessen competition between the corporation whose stock is so acquired and the corporation making the acquisition, or to restrain such commerce in any section or community, or tend to create a monopoly of any line of commerce."

[11] 26 Stat. 209-10 (1890). The text thereof may be found in 15 U. S. C. §§ 1-7.

[12] See Sen. Rep. No. 698, 63rd Cong., 2d Sess., p. 1 (1914).

[13] 280 U. S. 291, 50 S. Ct. 89, 74 L. Ed. 431 (1930).

to such a degree as will injuriously affect the public.''[14] As subsequent cases continued this interpretation, the ''substantially lessen'' phrase was emptied of any intelligible significance apart from the meaning it possessed under the Sherman Act.

With this experience in mind, Congress, by enacting the 1950 amendment to Section 7, made it quite clear that the test of legality to be applied to mergers under the Clayton Act was not the Sherman Act ''rule-of-reason'' but rather a stricter and a more inclusive test.[15] Those who support the Standard Stations doctrine often cite, in support of their advocacy, a House Committee Report on the amendment which states that ''a merger or acquisition will be unlawful if it may have the effect of either (a) substantially lessening competition or (b) tending to create a monopoly. These two tests of illegality are intended to be similar to those which the courts have applied in interpreting the same language in other sections of the Clayton Act. Thus, it would be unnecessary for the Government to speculate as to what is in the 'back of the minds' of those who promote a merger; or to prove that the acquiring firm had engaged in actions which are considered to be unethical or predatory; or to show that as a result of a merger the acquiring firm had already obtained such a degree of control that it possessed the power to destroy or exclude competitors or fix prices.''[16]

The reference therein to interpretations by the courts ''of other sections of the Clayton Act'' is believed, by many, to indicate that the House Committee had the Standard Stations case in mind when it drafted this report for that case had been decided two months before publication of the report, with the lower court decision antedating it by some fourteen months.[17] The Senate Committee, by contrast, although referring to the case in two places, states: ''It is expected that, in the administration of the act, full consideration will be given to all matters bearing upon the maintenance of competition, including the circumstances giving rise to the acquisition.''[18]

If one is willing to grant that Congress had knowledge of the decision at the time it amended Section 7 of the Clayton Act, the argument then proceeds that Congress, by the use of language grammatically identical

14 280 U. S. 291 at 298, 50 S. Ct. 89, 74 L. Ed. 431 at 441.

15 Sen. Rep. No. 1775, 81st Cong., 2d Sess., p. 4 (1950).

16 H. R. Rep. No. 1191, 81st Cong., 1st Sess., p. 8 (1949).

17 Others, however, feel that the report was prepared prior to the release of the Supreme Court opinion, so believe it in no way rests on, nor endorses, the views of the court. See McLaren, "Related Problems of 'Requirements' Contracts and Acquisitions in Vertical Integration," 45 Ill. L. Rev. 141 (1950), particularly p. 171.

18 Sen. Rep. No. 1775, 81st Cong., 2d Sess., p. 8 (1950).

to that found in Section 3, indicated a legislative intent to incorporate the doctrine of the case into the new section for, if it contemplated or desired a different test, then it is difficult to imagine why it did not choose to express this intent in contrasting language.[19] One looking closely at the 1950 amendment could well concede that its very words might show an intention to include the "quantitative substantiality test" envisioned in the Standard Stations doctrine. The new section is a prohibitory statute; it makes unlawful an acquisition where "the effect of such acquisition may be substantially to lessen competition, or tend to create a monopoly," but it does not compel the judiciary to decide whether any given merger is a "good" merger or a "bad" merger, *i. e.*, one for or against the public interest. Instead, it superficially purports to strike at any merger where the effect thereof would be to destroy competition in a substantial portion of the market.[20]

A different approach to the subject is disclosed in the matter entitled *Pillsbury Mills, Inc.*, where the Federal Trade Commission had occasion to consider at length the intent and scope of amended Section 7. The matter came before the Commission on an appeal from a trial examiner's report directing the dismissal of a complaint challenging the acquisition by Pillsbury Mills of the assets of two of its competitors. The Commission, having first determined the market area involved, undertook a consideration of the effect of these mergers on the sales of Pillsbury and on the share of the market occupied by the merged corporation[21] and found that Pillsbury, in the area, had gone from fifth place to second with respect to family flour; from third place to first as to bakery flour; and had retained its first place position as to mixes. Mill capacity and sales on a nationwide basis were also considered.[22] The Commission then concluded that, unless

[19] Schwartz, "Potential Impairment of Competition—The Impact of *Standard Oil Co. of California* v. *United States* on the Standard of Legality under the Clayton Act," 98 U. of Pa. L. Rev. 10 (1949).

[20] It should be noted, before leaving the direct discussion of the more strict test of the legality of corporate mergers, that Congress has clearly indicated that the Section 7 test, whether it be the strict one or one less strict, is to be applied to small acquisitions as well as to larger ones, particularly so when small acquisitions are shown to be a part of a pattern of acquisitions: H. R. Rep. No. 1191, 81st Cong., 1st Sess., p. 8 (1949); Sen. Rep. No. 1775, 81st Cong., 2d Sess., p. 5 (1950); and "The Merger Movement, A Summary Report," Federal Trade Commission, pp. 6-7 (1948).

[21] The area covered the Southeast United States in which Pillsbury's sales of bakery flour had increased 40%, its sales of mixes had increased 78%, its sales of family flour had increased 154%, and its sales of feed had gone from 20,000 tons to 175,000 tons per year.

[22] It appeared, from the opinion of the Commission, that Pillsbury had acquired nine mills, elevators, and similar facilities over the course of the prior ten years, causing the Commission to lay particular emphasis on the declining number of mills and the declining mill capacity, particularly in the market area where there was a comparative lack of competition in urban locations. Claims by Pillsbury that the evidence disclosed the presence of a large number of small competitors was offset, to some extent, by the fact these competitors were concentrated in rural areas.

these facts were rebutted, there appeared to be sufficient evidence to establish that competition in the urban centers of the market area had undergone a considerable change, leading to a fear that the trend, if continued, would lead to oligopolistic competition which, while perhaps not forbidden by the Sherman Act, was of the type which Congress intended to condemn and desired to halt when it enacted the 1950 amendment to Section 7.

When it turned to an examination of the legal aspects of the Pillsbury acquisitions, however, the Commission rejected a proposal that it should apply the Standard Stations doctrine to a case based on Section 7, saying that much "as the simplified test laid down in *Standard Stations* and *International Salt* may aid in the presentation of proof in cases under Section 3, it is not in itself a reliable guide for the Commission in carrying out its long-run responsibility to prevent reductions in competition through acquisitions."[23] It similarly rejected the "rule-of-reason" test of the Sherman Act, conceiving that Section 7 differed from the Sherman Act to the extent that a violation of the former could be established by a lower standard of proof even in relation to the same kind of acts as would be prohibited by the Sherman Act itself. In that connection, Chairman Howrey expressed the view that amended Section 7 "sought to reach the mergers embraced within its sphere in their incipiency, and to determine their legality by tests of its own. These are not the rule of reason of the Sherman Act, that is, unreasonable restraint of trade, nor are Section 7 prohibitions to be added to the list of *per se* violations. Somewhere in between is Section 7, which prohibits acts that 'may' happen to a particular market, that looks to a 'reasonable probability,' to 'substantial' economic consequences, to acts that 'tend' to a result. Overall is the broad purpose to supplement the Sherman Act and to reach incipient restraints."[24]

Critics of the doctrine so enunciated by Chairman Howrey question its "somewhere in between" position. They believe that the doctrine is a "rule-of-reason" approach if not a "rule-of-reason" test,[25] but the Attorney General's National Committee to Study the Antitrust Laws approved the test so propounded and urged that Section 7, as amended,

23 F. T. C. Docket 6000, pp. 8-9 (1953).

24 Ibid., p. 13. The Commission relied heavily on the opinion of the Court of Appeals in Transamerica Corp. v. Board of Governors, 206 F. (2d) 163 (1953), cert. den. 346 U. S. 901, 74 S. Ct. 225, 98 L. Ed. 401 (1953). It should be noted that while this was a Section 7 case and was decided in 1953, it was based on the section as it stood prior to the 1950 amendment so it must be supposed the court did not give consideration to the legislative history of the amendment when it drew its conclusions.

25 In support of this criticism, those opposing the doctrine point to a remark by Chairman Howrey to the effect that, at the Federal Trade Commission, "I am glad to say, we have moved in the direction of a rule of reason approach in our recent decisional work." See paper entitled "Coalescence of Legal and Economic Concepts of Competition," in CCH Antitrust Law Symposium (1955), pp. 5-6.

calls for a detailed analysis of all relevant economic factors. For that reason, the committee expressly rejected the "quantitative substantiality test" of the Standard Stations case.[26]

Until the law becomes clear on the point, the question is really one as to whether or not the conflicting doctrines of the Standard Stations and the Pillsbury Mills cases can or should be reconciled. A middle ground might be achieved without doing violence to either doctrine by the enactment of further legislation which could take into consideration the valid policy considerations of both. Such a law might require that a respondent's economic evidence be considered by the trial court or the trial examiner and that findings be based thereon. But, once it had been established that a given acquisition had affected a substantial share of the market, the risk of non-persuasion could be placed upon the respondent to show, by clear and convincing evidence, that the acquisition had not tended to lessen competition nor served to create a monopoly.[27] By making this allocation of the burdens between the parties, some of the objections to a full consideration of economic data that have been raised by proponents of the Standard Stations doctrine would be answered. The petitioner would not be required to supply conclusive proof that the acquisition had actually reduced competition below the level which it would otherwise have reached or maintained, nor would the court be required to make a nice evaluation as to the preponderance of evidence with respect to the respondent's affirmative defense. True, the court would have to deal with technical economic data, but it need not find for respondent unless it had been clearly convinced as to the merit of the defense presented so, unless the respondent had decisively made out this affirmative defense, the court would be justified in finding for the petitioner.

This formula, of course, would satisfy neither the adherents of the Standard Stations doctrine nor the proponents of the Pillsbury Mills view; the former would, without doubt, object to a federal court giving consideration to complex economic factors, and the latter would object to the placing of the burden of proof on the respondent. But some middle point must be achieved for the alternatives are either a proscription against all acquisitions or an ineffective and unenforcible antitrust law.

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26 Report of the Attorney General's Committee to Study the Antitrust Laws (1955), p. 123.

27 Oppenheim, "Federal Antitrust Legislation: Guideposts to a Revised National Antitrust Policy," 50 Mich. L. Rev. 1139 (1952). See also note in 63 Yale L. J. 233, where the writer, at p. 239, suggests that such a formula would "combine the judicial insights embodied in the Sherman Act rule-of-reason" with the Standard Stations doctrine.